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2554
No. 12055

United States
Court of Appeals
for the Ninth Circuit

JAMES G. SMYTH, Collector of Internal Revenue
of the First Internal Revenue Collection District
of California,

Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,

Appellee.

Transcript of Record

Appeal from the United States District Court
for the Northern District of California,
Southern Division

NOV 23 1948

No. 12055

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of the First Internal Revenue Collection District
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CIATION, a corporation,

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San Francisco, California,

Attorneys for Plaintiff and Appellee.

In the District Court of the United States, in and
for the Northern District of California, South-
ern Division

Civil No. 26017-S

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a Corporation,

Plaintiff,

vs.

JAMES G. SMYTH, Collector of Internal Revenue
of the First Internal Revenue Collection District
of California,

Defendant.

COMPLAINT FOR RECOVERY OF INCOME
AND EXCESS-PROFITS TAXES ILLE-
GALLY ASSESSED AND COLLECTED

Comes now the Plaintiff and, for cause of action
against Defendant, alleges:

I.

That Plaintiff is, and at all times herein men-
tioned was, a corporation organized and existing
under and by virtue of the laws of the State of
California, duly qualified to transact business
therein and having its principal place of business
and office at 150 Van Ness Avenue, San Francisco
2, California, and within the First Internal Reve-
nue Collection District of said State of California.

II.

That Defendant is now and at all times since
the 14th day of May, 1945, has been the duly ap-

pointed, qualified and acting Collector of Internal Revenue for the First Internal Revenue Collection District of California. That Defendant is the person to whom the income and excess-profits taxes, [1*] together with interest, the sums herein sought to be recovered, were paid by the Plaintiff, as hereinafter set forth. That at all times herein mentioned, Defendant was and still is a resident of the City and County of San Francisco, State of California, and of said Northern District of California, Southern Division.

III.

That jurisdiction of this Court exists under Title 28 U.S.C.A., Section 41 (5), and under Section 3772 (a)(2) of the Internal Revenue Code.

IV.

That since the inception of Federal income taxation in 1913, Plaintiff had been exempt from the imposition of any Federal income and/or excess-profits taxes until it was finally advised by the Commissioner of Internal Revenue in a letter dated July 27, 1945, copy of which is attached hereto and made a part hereof, marked "Exhibit 1", that further exemption from such taxation was denied and that the Plaintiff would be required to file income tax returns and pay any tax shown to be due thereon for each of its taxable years beginning on or after January 1, 1943.

V.

That only because of the requirement by the Commissioner of Internal Revenue, as aforesaid,

*Page numbering appearing at foot of page of original certified Transcript of Record.

for the filing of said tax returns, did the Plaintiff file income and excess-profits tax returns, and then under protest, and pay the amount of income and excess-profits taxes shown to be due thereon, together with accumulated interest upon said taxes. Federal tax returns for the calendar years 1943 and 1944, respectively, were accordingly filed on the respective forms provided for such purposes, by Plaintiff with Defendant, as Collector of Internal Revenue for the First District of California, on September 14, 1945, and the following taxes were paid at the time said returns were so filed:

For the year 1943, income tax in the amount of \$27,633.38;

For the year 1943, excess-profits tax in the amount of \$129,178.22;

For the year 1944, income tax in the amount of \$36,844.39;

For the year 1944, excess-profits tax in the amount of \$23,306.42 [2]

VI.

FIRST CAUSE OF ACTION

For a first cause of action against Defendant, Plaintiff alleges that the income tax for the year 1943 paid by Plaintiff to Defendant in the amount of \$27,633.38 on September 14, 1945, together with interest thereon paid the Defendant in the amount of \$2,485.11 on October 23, 1945, were illegally collected from the Plaintiff, and that no amount of income tax was legally due and owing from the Plaintiff by reason of the following facts:

(a) That Plaintiff was incorporated under the laws of the State of California on September 4, 1907, and until finally required by the aforesaid letter from the Commissioner of Internal Revenue, dated July 27, 1945, ("Exhibit 1"), to file income tax returns as aforesaid, had been exempt from the payment of any Federal income and/or excess-profits taxes.

(b) That in furtherance of the purpose for which it was originally organized as an automobile club, Plaintiff has provided during the years 1943 and 1944, as well as prior and subsequent to said years, (1) a Touring Bureau which provides the members with complete touring data and assists them in planning motor trips; (2) an emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter automobile trouble on the highways; (3) a Road Sign Department, which operates in conjunction with state and local authorities a service consisting of the erection and maintenance of direction and warning signs and historical markers; (4) a Public Safety Department which carries on an active and aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions; (5) an Adjustment and Traffic Department, which advises and assists the members with respect to traffic violations and accidents; (6) a License Department which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtaining auto-

mobile license plates, as well as Federal auto tax stamps; and (7) a Magazine Department which publishes and distributes to the members a magazine, keeping them informed of motoring conditions and improvements, and specializing [3] in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no paid advertising material since January 1, 1942.

VII.

That Section 101(9) of the Internal Revenue Code, in force during the years 1943 and 1944, as well as prior and subsequent thereto, provides exemption from income tax on qualifying corporations in the following language:

“Clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.”

That Plaintiff is an automobile club organized and operated exclusively for the pleasure and recreation of its members and for other non-profitable purposes, and that no part of Plaintiff's earnings inure to the benefit of any private shareholder or member.

VIII.

That the whole purpose of the organization of Plaintiff was to provide, by association and cooperation among its members, for the achievement of its prime objective, namely, the pleasure and recreation of the passenger-car owners constituting

its membership, by the improvement and marking of roads, obtaining legislation to further the construction of more and better highways, and furnishing travel information and guidance and assistance to its members, all on a non-profit basis.

IX.

That during the years 1943 and 1944, and for a number of years prior and subsequent thereto, Plaintiff has operated as an automobile club with a board of directors made up of 21 members which meets regularly every month throughout the year, with the exception of the month of July when there is no meeting due to the usual vacation period, and each year the board of directors appoints ten committees made up of from 5 to 9 members each, the names of which committees are as follows:

Executive Committee—Finance Committee—Legislative Committee—Good Roads Committee—Emergency Road Service Committee—Public Safety [4] Committee—Membership Committee—Publicity Committee—Transcontinental Highway Committee, and Forestry Committee.

X.

That the California State Automobile Association Inter-Insurance Bureau, a reciprocal inter insurance exchange, which is an entirely separate and distinct organization and entity from Plaintiff, was formed some years ago and is operated by and on their own particular behalf, and not on behalf of Plaintiff, by a group of members of Plaintiff Association for the purpose of providing indemnity among themselves, that is, the individual subscrib-

ers to the said Bureau, who desire to protect themselves against various automobile hazards, the exchange of indemnity being effected by an agent holding a power of attorney for that purpose from each individual in said group; that Plaintiff and the said Bureau, each with its own staff of employees, occupy common quarters and share the expense of same; that they also share certain other expenses when, for convenience, an employee of one organization also performs services for the other, but neither Plaintiff nor the said Bureau derives any profit whatsoever from the operation of the other.

XI.

That Plaintiff was not during 1943 or 1944, or at any other time, organized or operated for the purpose of rendering services of a purely commercial nature to its members, and the great majority of such services are not obtainable by members commercially at any cost.

XII.

That on or about October 23, 1945, and within two years of the date of payment of the aforesaid amount of \$27,633.38 as income taxes for the year 1943, and the payment on October 23, 1945, of interest in the amount of \$2,485.11, making a total of \$30,118.49, erroneously and illegally collected as aforesaid, Plaintiff filed its claim for refund on Form 843 for the calendar year 1943, a true copy of which is attached hereto and made a part hereof, marked "Exhibit 2". Said claim set forth, under oath, the grounds for refund hereinabove relied

upon and facts sufficient to apprise the Defendant and the Commissioner of Internal Revenue of the exact basis of the claim. Since the [5] Commissioner of Internal Revenue has rendered no decision on said claim within the period of six months from the date of filing said claim, this suit for refund is brought under the authority and in accordance with the provisions of Section 3772 (a)(2) of the Internal Revenue Code.

XIII.

That by reason of the above facts, Defendant erroneously and illegally collected \$27,633.38 in income taxes from Plaintiff, together with \$2,485.11 interest thereon to date of payment, making a total of \$30,118.49, for the year 1943, all of which Defendant has refused and still does refuse to repay or refund to Plaintiff, notwithstanding Plaintiff has made demands and claims therefor according to law.

SECOND CAUSE OF ACTION

For a second and separate cause of action against Defendant, Plaintiff further alleges:

XIV.

The allegations contained in paragraphs I to V inclusive, are hereby fully and completely incorporated herein by reference in this cause of action.

XV.

That the excess-profits tax for the year 1943 paid by Plaintiff to Defendant in the amount of \$129,178.22 on September 14, 1945, together with interest thereon paid to Defendant in the amount of \$11,617.19 on October 23, 1945, were illegally col-

lected from the Plaintiff, and that no amount of excess-profits tax was legally due and owing from the Plaintiff, by reason of the facts stated herein under the First Cause of Action in paragraph VI (a) and (b) and paragraphs VII to XI inclusive, all of which are hereby fully and completely incorporated herein by reference in this Second Cause of Action.

XVI.

That on or about October 23, 1945, and within two years of the date of payment of the aforesaid amount of \$129,178.22 as excess-profits tax for the year 1943, and the payment on October 23, 1945, of interest in the amount of \$11,617.19, making a total of \$140,795.41, erroneously and illegally collected [6] as aforesaid, Plaintiff filed its claim for refund on Form 843 for the calendar year 1943, a true copy of which is attached hereto and made a part hereof, marked "Exhibit 3". Said claim set forth, under oath, the grounds for refund hereinabove relied upon and facts sufficient to apprise the Defendant and the Commissioner of Internal Revenue of the exact basis of the claim. Since the Commissioner of Internal Revenue has rendered no decision on said claim within the period of six months from the date of filing said claim, this suit for refund is brought under the authority and in accordance with the provisions of Section 3772 (a)(2) of the Internal Revenue Code.

XVII.

That by reason of the above facts, Defendant erroneously and illegally collected \$129,178.22 in

excess-profits taxes from Plaintiff, together with \$11,617.19 interest thereon to date of payment, making a total of \$140,795.41, for the year 1943, all of which Defendant has refused and still does refuse to repay or refund to Plaintiff, notwithstanding Plaintiff has made demands and claims therefor according to law.

THIRD CAUSE OF ACTION

For a third and separate cause of action against Defendant, Plaintiff further alleges:

XVIII.

The allegations contained in paragraphs I to V inclusive are hereby fully and completely incorporated herein by reference in this cause of action.

XIX.

That the income tax for the year 1944 paid by Plaintiff to Defendant in the amount of \$36,844.39 on September 14, 1945, together with interest thereon paid to Defendant in the amount of \$1,102.81 on October 23, 1945, were illegally collected from the Plaintiff, and that no amount of income tax was legally due and owing from the Plaintiff by reason of the facts stated herein under the First Cause of Action in paragraph VI (a) and (b) and paragraphs VII to XI inclusive, all of which are hereby fully and completely incorporated herein by reference in this Third Cause of Action.

XX.

That on or about October 23, 1945, and within two years of the date of payment of the aforesaid amount of \$36,844.39 as income tax for the year 1944, and the payment on October 23, 1945, of in-

terest in the amount of \$1,102.81, making a total of \$37,947.20, erroneously and illegally collected as aforesaid, Plaintiff filed its claim for refund on Form 843 for the calendar year 1944, a true copy of which is attached hereto and made a part hereof marked "Exhibit 4". Said claim set forth, under oath, the ground for refund hereinabove relied upon and facts sufficient to apprise the Defendant and the Commissioner of Internal Revenue of the exact basis of the claim. Since the Commissioner of Internal Revenue has rendered no decision on said claim within the period of six months from the date of filing said claim, this suit for refund is brought under the authority and in accordance with the provisions of Section 3772 (a)(2) of the Internal Revenue Code.

XXI.

That by reason of the above facts, Defendant erroneously and illegally collected \$36,844.39 in income taxes from Plaintiff, together with \$1,102.81 interest thereon to date of payment, making a total of \$37,947.20, for the year 1944, all of which Defendant has refused and still does refuse to repay or refund to Plaintiff, notwithstanding Plaintiff has made demands and claims therefor according to law.

FOURTH CAUSE OF ACTION

For a fourth and separate cause of action against Defendant, Plaintiff further alleges:

XXII.

The allegations contained in paragraphs I to V inclusive, are hereby fully and completely incorporated herein by reference in this cause of action.

XXIII.

That the excess-profits tax for the year 1944 paid by Plaintiff to Defendant in the amount of \$23,306.42 on September 14, 1945, together with interest thereon paid to Defendant in the amount of \$697.60 on October 23, 1945, [8] were illegally collected from the Plaintiff, and that no amount of excess-profits tax was legally due and owing from the Plaintiff, by reason of the facts stated herein under the First Cause of Action in paragraph VI (a) and (b) and paragraphs VII to XI inclusive, all of which are hereby fully and completely incorporated herein by reference in this Fourth Cause of Action.

XXIV.

That on or about October 23, 1945, and within two years of the date of payment of the aforesaid amount of \$23,306.42 as excess-profits tax for the year 1944, and the payment on October 23, 1945, of interest in the amount of \$697.60, making a total of \$24,004.02, erroneously and illegally collected as aforesaid, Plaintiff filed its claim for refund on Form 843 for the calendar year 1944, a true copy of which is attached hereto and made a part hereof marked "Exhibit 5". Said claim set forth, under oath, the grounds for refund hereinabove relied upon and facts sufficient to apprise the Defendant and the Commissioner of Internal Revenue of the exact basis of the claim. Since the Commissioner of Internal Revenue has rendered no decision on said claim within the period of six months from the date of filing said claim, this suit for refund is

brought under the authority and in accordance with the provisions of Section 3772 (a)(2) of the Internal Revenue Code.

XXV.

That by reason of the above facts, Defendant erroneously and illegally collected \$23,306.42 in excess profits taxes from Plaintiff, together with \$697.60 interest thereon to date of payment, making a total of \$24,004.02, for the year 1944, all of which Defendant has refused and still does refuse to repay or refund to Plaintiff notwithstanding Plaintiff has made demands and claims therefor according to law.

Wherefore, Plaintiff prays this Honorable Court for judgment that the Plaintiff was exempt from the payment of income tax, as well as excess-profits tax, under Section 101(9) of the Internal Revenue Code for the years 1943 and 1944, and that Plaintiff has overpaid its liability for income taxes and interest thereon, as well as excess-profits taxes and interest thereon, for [9] the calendar years 1943 and 1944, in the following amounts:

For the year 1943, income tax in the amount of \$27,633.38, and interest in the amount of \$2,485.11, making a total of \$30,118.49;

For the year 1943, excess-profits tax in the amount of \$129,178.22, and interest in the amount of \$11,617.19, making a total of \$140,795.41;

For the year 1944, income tax in the amount of \$36,844.39, and interest in the amount of \$1,102.81, making a total of \$37,947.20;

For the year 1944, excess-profits tax in the amount of \$23,306.42, and interest in the amount of \$697.60, making a total of \$24,004.02; and

That Plaintiff have and recover from Defendant the total amount of \$232,865.12 plus interest thereon from the dates of overpayment as provided by law; and for such further relief as may be meet and just.

/s/ GEORGE E. SANDFORD,
Attorney for Plaintiff.

(Duly Verified.) [10]

“EXHIBIT 1”

Copy

Treasury Department
Washington 25

Office of the Commissioner of Internal Revenue

Address reply to Commissioner of Internal Revenue and refer to IT:P:T:1 FDF

Jul 27 1945

California State Automobile Association
150 Van Ness Avenue
San Francisco, California

Gentlemen:—

Reference is made to the request of your attorney, Mr. A. H. Deibert, that the Bureau's ruling of September 23, 1944, holding that you are not entitled to exemption from Federal income tax under the provisions of section 101(9) of the Internal Revenue Code be reconsidered, in support of which request a brief was filed with this office by Mr. Deibert during the early part of this year.

Careful consideration has been given to the statements and arguments made by Mr. Deibert and to the cases cited by him in support of his contention that you are entitled to the exemption provided in the law and it has been concluded that the ruling contained in Bureau letter of September 23, 1944, should not be disturbed.

In the letter of September 23, 1944, which was approved by the Acting Secretary of the Treasury, it was stated that the ruling contained in that letter would not be applied to taxable years beginning prior to January 1, 1943. During May 1945 Mr. Deibert was advised orally of the conclusion that the ruling of September 23, 1944, holding that you are not entitled to exemption, should not be disturbed and on June 14, 1945, he addressed a letter to this office requesting, for reasons stated therein, that the ruling be not applied to taxable years begun prior to January 1, 1945.

Mr. Deibert stated that you have had a tax exempt status throughout your existence which began some years prior to March 1, 1913, and that it is inequitable to apply the adverse ruling retroactively to January 1, 1943, in view of the fact that the Bureau first raised the question of your exemption by letter to you from the collector of internal revenue at San Francisco dated September 10, 1941, and that the information requested in that letter was furnished on October 5, 1941, but that it was not until about October 1, 1944, that you received the ruling of September 23, 1944, advising that you are held not entitled to tax exemption.

The records of the Bureau fail to show that you filed proof of exemption or otherwise requested a ruling on your exempt status, or were ever held by this Bureau to be entitled to exemption from Federal income tax prior to September 10, 1941, when you were requested by the collector to furnish information for use in determining whether you are entitled to exemption.

Prior to the time that the information submitted by you in 1941, was taken up for consideration a substantial number of automobile clubs had been held to be [11] entitled to exemption under section 101(9) of the Internal Revenue Code and prior revenue acts. While the information submitted to you was under consideration in this office, it was decided to reexamine the general question of whether an automobile club or association having the usual purposes and activities is entitled to the exemption provided in section 101(9) in connection with a particular case, and in G.C.M. 23688 (C.B. 1943, 283) it was concluded for the reasons therein stated that the subject automobile association is not entitled to the exemption. This opinion was first published during the first part of July 1943, after which the information submitted by you during October 1941 was again taken up for consideration in the light of the view expressed in that General Counsel's memorandum, and it was concluded with the concurrence of the Chief Counsel and the approval of the then Acting Secretary of the Treasury that you are not entitled to the exemption provided in section 101(9) and that under

authority granted by section 3791(b) of the Internal Revenue Code the ruling would not be applied to years begun prior to January 1, 1943.

Since the letter to you from the collector of internal revenue dated September 10, 1941, requesting information for use in determining whether you are entitled to exemption from tax was notice to you that your right to exemption was being questioned by the Bureau and, as G.C.M. 23688, *supra*, was first published almost six months prior to the close of 1943, it is the view of this Bureau that you were on notice that your right to exemption was at least doubtful in ample time for you to make proper provisions for the payment of any tax due for 1943 and subsequent years. Application of the ruling of September 23, 1944, to 1943 and subsequent years is therefore deemed to be both equitable and fair and it will not be disturbed. Accordingly, you will be required to file income tax returns and pay any tax shown to be due thereon for each of your taxable years beginning on or after January 1, 1943.

Very truly yours,

/s/ JOSEPH D. NUNAN, JR.,
Commissioner. [12]

EXHIBIT No. 2

Form 843 Treasury Department Internal Revenue
Service (Revised April 1940)

Copy

CLAIM

To be filed with the Collector where assessment
was made or tax paid

The Collector will indicate in the block below the
kind of claim filed, and fill in the certificate on the
reverse side.

☒ Refund of Tax Illegally Collected.

☐ Refund of Amount Paid for Stamps Un-
used, or Used in Error or Excess.

☐ Abatement of Tax Assessed (not applicable
to estate or income taxes).

State of California,

City and County of San Francisco—ss:

Name of taxpayer or purchaser of stamps, Cali-
fornia State Automobile Association.

Business address, 150 Van Ness Avenue—San
Francisco 2, California.

Residence,

The deponent, being duly sworn according to law,
deposes and says that this statement is made on
behalf of the taxpayer named and that the facts
given below are true and complete:

1. District in which return (if any) was filed,
1st California.

2. Period (if for income tax, make separate
form for each taxable year) from January 1, 1943,
to December 31, 1943.

Exhibit No. 2—(Continued.)

3. Character of assessment or tax, Income Tax.

4. Amount of assessment, \$30,118.49; dates of payment, Sept. 14, 1945, \$27,633.38; Oct. 23, 1945, \$2,485.11.

5. Date stamps were purchased from the Government,

6. Amount to be refunded, \$30,118.49.

7. Amount to be abated (not applicable to income or estate taxes),

8. The time within which this claim may be legally filed expires, under Section 322 IRC, on September 14, 1948.

The deponent verily believes that this claim should be allowed for the following reasons:

See Statement Attached.

/s/ CALIFORNIA STATE AUTO-
MOBILE ASSOCIATION,

By D. E. WATKINS,

Sec'y. & Gen. Mgr.

Sworn to and subscribed before me this 23rd day of October 1945.

CON T. SHEA,

(Signature of officer administering oath)

Notary Public in and for the City and County of San Francisco, State of California. [13]

STATEMENT

I.

The California State Automobile Association, with general offices at 150 Van Ness Avenue, San Francisco, California, was incorporated September 4, 1907, and until a letter addressed to it on

Exhibit No. 2—(Continued.)

September 23, 1944, by the Commissioner of Internal Revenue, had been exempt from the imposition of any Federal income taxes. That letter not only withdrew such exemption, but applied the ruling for years beginning with the calendar year 1943, notwithstanding the fact that notice of the withdrawal of such exemption was not received by the Association until the latter part of the year 1944.

This Association was originally organized as a non-profit, non-stock corporation and its main object and purpose is, and always has been, to furtherance of the pleasure and recreation of its members. Its aims as set forth in its articles of incorporation are all directed to such main purpose and all of its activities have been designed to contribute to that end.

In accomplishing the purpose for which it was organized, and for which it is now, and always has been operated, the Association provides (1) a Touring Bureau which provides the members with complete touring data and assists them in planning motor trips; (2) an Emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter automobile trouble on the highways and relieves the members from the worries and anxieties which might otherwise interfere [14] with their pleasure and recreation while motoring; (3) a Road Sign Department, which operates in conjunction with State and local authorities and which benefits not only the members of the Association but the public as a whole by erecting and maintain-

Exhibit No. 2—(Continued.)

ing direction and warning signs and historical markers; (4) a Public Safety Department which carries on an active and aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions; (5) an Adjustment and Traffic Department, which advises and assists the members with respect to traffic violations and accidents; (6) a License Department which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtains automobile license plates, as well as the Federal Tax Stamps now required; and (7) a Magazine Department which publishes and distributes to the members a magazine keeping them informed of motoring conditions and improvements, and specializing in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no advertising material whatever for the past several years.

It is important to note that the Association itself does not maintain or operate an insurance Bureau nor does it write insurance itself, or operate a department or bureau for placing the same. Also, it does not engage in any way in financing the purchase of automobiles, nor does it engage in or operate a Department or Bureau engaging in any activity normally carried on by ordinary business organizations for profit. It is consequently neither engaged in nor in competition with commercial enterprises. Further, it does not engage in or make

Exhibit No. 2—(Continued.)

any arrangements for its members to participate in any plan by which members may obtain discounts on supplies or services of any nature whatsoever. [15]

It is also important to note that no block memberships are issued to companies or other organizations owning and operating a number of passenger motor cars, but a membership is issued in connection with the operation of each passenger car.

The main source of the Association's income is represented by the dues and initiation fees paid by its members, and any other income received has its origin either in the ownership or control of Association property and is purely an incident to said ownership, or in connection with matters incident to the furtherance and accomplishment of the main purpose for which the Association was organized, and for which it is and has been operated. All of the earnings of the Association are employed to further such main purpose and no part of the net earnings inure to the benefit of any member.

In order that there would be no occasion whatever for considering that the Association might have income of a nature which might conceivably deprive it of its tax exempt status, the Association several years ago eliminated entirely all income resulting from advertisement in its magazine, entitled "Motorland", and even refused to continue renting a garage on the rear of its property from which a small monthly rental was derived, leaving

Exhibit No. 2—(Continued.)

the garage unoccupied since that time. The Association has been most meticulous in the observance of every requirement which it conceived might be placed upon it for the maintenance of its tax exempt status.

It is believed, therefore, that the Association is definitely within the purview of Section 101 (9) of the Internal Revenue Code which provides exemption from income tax on corporations in the following language:

“Clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.” [16]

(A) The Association is a club organized exclusively for pleasure, recreation, and other non-profitable purposes.

In the Commissioner's aforesaid letter of September 23, 1944, it is stated that the opinion of the Bureau is that this Association is not a “club” within the meaning of Section 191 (9) of the Internal Revenue Code and/or corresponding provisions of prior revenue acts. This opinion appears to be based in part at least upon the decision of the District Court of the United States for the Southern District of California, Central Division, in the case of *Arner v. Rogan* (May 20, 1944, CCH P. 9567), and upon a statement that although there is no statutory definition of the term “club” as used in Section 101 (9) of the Code, it is believed that

Exhibit No. 2—(Continued.)

the term “contemplates a commingling of members, one with the other in fellowship”.

It is believed that the case of *Arner v. Rogan* has no proper application to the question at issue here, viz., whether this Association is exempt from Federal income tax, and the question of commingling of members in fellowship is in no sense required in connection with the activities of a club of this character.

It is believed further that in reaching the conclusion stated in the Commissioner's letter of September 23, 1944, there has been an unfortunate confusion of two entirely separate and distinct provisions of the Internal Revenue Code, and that one has no proper relationship to the other so far as the matter as issue is concerned.

In the first place, it should be pointed out that *Arner v. Rogan* dealt with the imposition of a tax on dues under Section 501 of the Revenue Act of 1926 as amended in 1928, the counterpart of which at present is Section 1710 of the Code which provides, so far as pertinent, as follows: [17]

“(a) Rate—There shall be levied, assessed, and paid—

“(1) Dues or membership fees.—A tax equivalent to 11 per centum of any amount paid as dues or membership fees to any social, athletic, or sporting club or organization, if the dues or fees of an active resident annual member are in excess of \$10 per year.” Emphasis supplied.)

Exhibit No. 2—(Continued.)

For purposes of comparison, Section 101 (9) of the Code is again quoted:

“Clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.”

Section 1710 of the Code is found under Chapter 10—Admissions and Dues, while Section 101 (9) is found in Chapter 1—Income Tax.

Section 1710 imposes an excise tax upon dues and membership fees of a specifically described type of club, but Section 101 (9) exempts from income tax certain designated corporations, including the clubs specified in subsection 9, within which category it is contended this Association falls.

There is, therefore, in the tax treatment of the divergent types of clubs respectively dealt with in Sections 1710 and 101 (9) no necessary or natural connection, and the descriptions of these two distinctive groups of clubs add further emphasis to the fact that they are not only not identical, but that the only thing they have in common is the generic term “club”.

There is no reference whatever in Section 101 (9) to social, athletic, or sporting clubs, which are the sole objects of taxation in Section 1710, and it is obvious from the most cursory consideration of the terms ‘pleasure’ and ‘recreation’ that both pleasure and recreation may be indulged in by persons acting individually and without any associa-

Exhibit No. 2—(Continued.)

tion whatever with other individuals. For example, one may engage in playing a game of solitaire as a means of pleasure or recreation, or one may also indulge in bicycling, fishing, or playing a game of golf by himself and derive both pleasure and recreation [18] from so doing, and in none of these instances, is association or commingling with any other individual necessary.

For the purposes of this argument, it may be admitted that the Southern California District Court was correct in holding in *Arner v. Rogan* that the Biltmore Health Club, which was there under consideration, was not a social, athletic or sporting club, and even that a commingling of members may be necessary to constitute such a club. At the same time, we vigorously deny that the same standard of definition must, or can properly be applied to an organization of the character of this Association, where commingling of members is not even in the remotest degree necessary to the pleasure and recreation of any individual member. Many other instances of indulging in pleasure and recreation, in addition to the several above referred to, might be cited where the desired pleasure and recreation is achieved by an individual entirely by himself and without the necessity of any association whatever with any other person. There are many individuals who take motor trips for pleasure or rest, to remote places to hunt, fish, hike and view scenic wonders. And this is particularly true in California where the climate makes all-year trips

Exhibit No. 2—(Continued.)

for pleasure and recreation possible. We believe it logically follows that the commingling or association of members, one with another, as in a social, athletic or sporting club, cannot be held to be a requirement in a club devoted to pleasure and recreation. For the reasons stated, we believe that the case of *Arner v. Rogan* has no application in the consideration of the case of this Association.

The Court in the *Arner* case was correct in stating that there has been no judicial definition of the words "club or organization" as used in the statute there under consideration. The Court then proceeded to say "It seems safe to say that at least there must be some sort of association or [19] cooperation between the members in an effort to reach some common objective before we may consider that there is a club or organization."

Regardless of the fact that such statement was made with reference to social, athletic or sporting clubs or organizations, with which we are not here concerned, it may be stated unequivocally that there is association and cooperation between the members of the California State Automobile Association "in an effort to reach some common objective". The whole purpose of the organization of this association was to provide, by association and cooperation among the members, for the achievement of its prime objective, namely, the pleasure and recreation of the passenger car owners constituting its membership, by the improvement and marking of roads, obtaining legislation to further the construc-

Exhibit No. 2—(Continued.)

tion of more and better highways, furnishing travel information and guidance to its members, etc. In that connection, it might be pointed out that this Association has a Board of Directors made up of 21 members which meets regularly every month throughout the year with the exception of the month of July, when there is no meeting due to the usual vacation period, and that each year the Board of Directors appoints 10 committees, made up of from 5 to 9 members each, the names of which committees are as follows: Executive Committee, Finance Committee, Legislative Committee, Good Roads Committee, Emergency Road Service Committee, Public Safety Committee, Membership Committee, Publicity Committee, Transcontinental Highway Committee, and Forestry Committee. The 21 Directors of the Association serve without compensation, but give considerable time to their duties as such Directors.

In the earlier days of motoring when this Association was conceived as a motor club in 1907 by a half dozen men, it was their enthusiasm for motoring as a means of pleasure and recreation that prompted them to give their time to the development of good roads, and the other purpose of the Association and since that time all succeeding Directors have been prompted [20] by the same idea in contributing their time without compensation in connection with their attendance at the monthly meetings of the Board and the interim meetings of the various committees, all to the end of improving road conditions and other facilities in connec-

Exhibit No. 2—(Continued.)

tion with motoring to make this form of recreation more pleasurable.

The Committees above-named not only have meetings of their own, but in many cases there is frequent contact by individual members with the chairmen of the respective Committees, so that there is almost constant association between members for the furtherance of the primary purposes for which the Association was organized, i.e., the pleasure and recreation of its members.

Consequently, even adopting the criterion applied to an entirely separate and different section of the Internal Revenue Code (1710) by the Court in *Arner v. Rogan*, it seems clear that this Association falls within the above quoted definition by the Court in that case of a "club".

As set forth in 25 Ruling Case Law, 45 et seq. the word "club" has no very definite meaning. However, clubs are formed for all sorts of purposes and there is naturally no uniformity in either their constitution or rules, but although the word "club" does not have a very definite meaning, it does of course have some meaning, and reference to Ruling Case Law supra, 11 Corpus Jur. 922, and note 1, 4 American Jurisprudence 456 et seq., and Websters New International Dictionary, 2nd Edition, Unabridged, reveals that a club is "any association of persons who have joined together for a certain object." Webster set forth among other definitions of the word "club" the following:

"To unite for a common end, or contribute to a common stock; as to club exertions."

Exhibit No. 2—(Continued.)

* * * *

Intransitive: "To form a club; to combine for the promotion of some common object; to unite." [21]

In so far as the Association is concerned, there can be no doubt that the members "combined for the promotion of some common object" and that such common object was the creation, improvement and maintenance of conditions and the dissemination of information, including maps, which would materially contribute to the pleasure and recreation of passenger car users, who were members of the Association, and which could be accomplished only by their combining together in the form of a club. Such object could not possibly be attained through the efforts of unassociated individuals.

It is hardly open to argument that concern over possible breakdowns on a highway, traffic conditions, proper routing, and possible consequences resulting from unexpected mishaps, etc. are not compatible with pleasure and recreation, nor is it open to argument that one individual or numerous individuals acting separately could do little, if anything, to improve conditions, to collect and distribute information covering large geographical areas, so as to further the pleasure and recreation of owners of passenger cars. The only solution for individuals desirous of using their passenger cars under conditions which would materially contribute to their pleasure in motoring, would be to join to-

Exhibit No. 2—(Continued.)

gether and as a group, association, or club, accomplish what otherwise would be beyond reach.

This the members of the Association have done, and accordingly it is maintained that this Association, consisting of persons who have joined together for the principal purpose of furthering the pleasure and recreation they derive from motoring, is a club organized exclusively for pleasure, recreation and other non-profitable purposes, within the purview of Section 101 (9) of the Code. [22]

(B) The Association is operated exclusively for pleasure and recreation and other non-profitable purposes.

Not only was the Association organized for the purpose stated, but a review of its activities, as set forth herein, establishes that such activities were conducted with but one end in view, namely, furtherance of the primary purpose, pleasure and recreation, for which the Association was organized and that as a practical matter, it was operated not only for the pleasure and recreation of its own members, but incidentally and inescapably for a similar non-profitable purpose, the benefit of the motoring public as a whole, which benefit naturally flowed from the activities of the Association on behalf of its members and which should, of course, in no degree affect the tax exempt status of the Association.

As will be demonstrated, the mere fact that the Association may realize some small incidental income from sources other than dues and initiation

Exhibit No. 2—(Continued.)

fees of its members, has no bearing upon its tax exempt status, inasmuch as the realization of such income is merely incidental to activities in pursuit of the accomplishment of the main purpose for which the Association was organized and is operated.

The Association and the Inter-Insurance Bureau, the latter an entirely separate organization, jointly occupy the headquarters of the Association at 150 Van Ness Avenue, San Francisco, California, and the Bureau reimburses the Association by the payment of rent for the space it occupies, based entirely upon its proportionate share of expenses covering the operation and maintenance of the building at that address. It is estimated that the Bureau occupies approximately two-thirds of the building and it is accordingly charged with such proportion of the cost of maintenance and operation. It should be emphasized, however, that this is merely an allocation of costs, and that the [23] Association derives no amount whatever as profit from the payment of such rent. There is likewise a reimbursement by the Bureau to the Association of the Bureau's proportionate share of certain other services which are used jointly by both organizations, such as, for example, salaries of the Purchasing Agent and Assistant, Storeroom, Mailing Department, Telephone and Switchboard, Lunch Room, Nurse and Tube Operators. It has been found that each of these two organizations, which are entirely separate and distinct entities, can jointly utilize the

Exhibit No. 2—(Continued.)

services of certain employees, resulting in a saving to each organization, and the proportionate parts of such salaries and expenses are accordingly charged to the Association and the Bureau, respectively, and when paid by the Association entirely are proportionately reimbursed by the Bureau. Again, there is no element of profit whatever involved in the payment of such expenses by the Bureau to the Association.

In the "Statement Regarding Activities of California State Automobile Association" furnished the Commissioner of Internal Revenue in September, 1941, and signed and sworn to by D. E. Watkins, Secretary of the Association, it is stated on page 8 thereof, that the only income received from non-members consisted of advertising in its magazine and a reimbursement from State and local authorities of the cost price of road sign material, and the rental of property for \$125 per month. In that connection, you are informed that no advertising revenue has been derived from the magazine "Motorland" since January 1, 1942, and since that date no advertising whatever has been accepted.

The rental of property at \$125 per month represents rental paid for the use of the garage on the premises of the general offices at 150 Van Ness Avenue, but the last rental for such garage was paid on October 3, 1941, and the garage has not been rented since that time, and has therefore completely ceased to be a source of income. [24]

With respect to the reimbursement by State and

Exhibit No. 2--(Continued.)

local authorities of the cost price of road sign material, it is stated on page 6 of the above-mentioned Statement that such reimbursement for the year 1940 amounted to \$100,248.18, and that the Association's expense, which it paid out of its own funds, for erecting and maintaining said signs for the year 1940, amounted to \$69,073.25. In that connection, it should be observed that the latter amount represents the sum expended by the Association over and above the amount of \$100,248.18, which was reimbursed to it by the State and the various cities and counties within the area in which it operates, so that the total amount expended for that year by the Association was approximately \$169,000, of which the Association was reimbursed only \$100,248.18. Obviously, there was not only no profit involved in that transaction, but an actual outlay of nearly \$70,000, with no reimbursement whatever, by the Association which constituted one of the services rendered its members with the objective of increasing their pleasure and recreation in motoring.

Attention is also invited to the fact that during the year 1943 there were approximately 153 officially designated hotels under contract with the Association and that during that year the Association received only \$129.15 for its endorsement of these hotels and although the receipt of this small amount, while actually taken in 1943, was really chargeable against endorsements in 1942. In 1944 the list of such hotels had dropped to 141, but

Exhibit No. 2—(Continued.)

no endorsement fees were charged in 1944 and none received. The association received \$265.00 in 1943 and \$275.00 in 1944 for endorsement of official garages.

A number of decided cases have held that the receipt of incidental income, even in some instances where the amounts were quite large, is not sufficient to destroy the tax exempt status of an organization otherwise [25] entitled thereto. In fact, the Supreme Court of the United States in *Trinidad v. Sagrada*, 263 U.S. 578, pointed out in a somewhat similar case that the statute says nothing about the source of the income, but makes its destination the ultimate test of exemption. That principle of law has been cited and followed by a number of Federal Courts in cases involving the application of Section 101 (9) of the Code. Applying that principle to this case, your attention is again invited to the sworn statement of Mr. Watkins in 1941, in which, on page 7, he made the following statements:

“Disposition of Income: The entire income of the Association is used to carry out the purposes recited in its Articles of Incorporation and to render to its members the various services previously enumerated. No distributions of income has ever been made to members nor does any profit inure to the benefit of any individual.”

The foregoing statement is as true today as when it was made and no profit will at any time inure to the benefit of any individual.

Exhibit No. 2—(Continued.)

A number of cases, as above indicated, have been litigated in the Federal Courts dealing with the exact question of the tax exempt status of such organizations under the revenue laws, and the Courts have repeatedly reached the conclusion that where the receipt of income was purely incidental to the main purpose of the organization in question, such fact was not sufficient to disturb the right to such exemption.

One of the outstanding cases of this type is *Koon Kreek Klub v. Thomas, et al.*, 106 F. 2d. 616, decided by the 5th Circuit Court of Appeals.

In that case the appellant was organized as a fishing and hunting club, maintaining a club house, boats, and fishing and game preserves for the pleasure and amusement of its members, and it acquired a tract of land containing 6777 acres, which completely surrounded a tract of 340 acres owned and occupied by one Thomas. It granted grazing privileges to Thomas for a consideration of \$500 per year, and for a certain period extended [26] similar privileges to its manager for \$100 per year. Prior to the tax years before the Court, the club received income from dues which averaged \$12,500 per year. Oil was later discovered about 7 miles from the club property and in 1934, one of the years under consideration, the club granted an oil lease on its entire property for a consideration of \$4.00 per acre, with an annual renewal rental of \$1.00 per acre, reserving the usual royalties. The lease was not renewed, however, and the amount received, which exceeded \$25,000, was used to reduce or retire a mortgage which had been outstanding

Exhibit No. 2—(Continued.)

against the property since its acquisition by the club.

The Court found that the question of tax liability turned upon the interpretation of Section 101 (9) of the Revenue Act of 1934, and held that whatever financial gain was realized from the grazing and leasing activities was incidental to and directed toward the accomplishment of the purpose upon which the income tax exemption was based.

The Court continued:

“The contention that the club did not operate exclusively for non-profitable purposes because of the leases of grazing rights is equally without foundation. In order to maintain its houses and preserves, it was required to raise funds from some source. That these funds might be derived from a use of the properties themselves, not inconsistent with the purposes for which they were maintained, would not change the nature of the operation any more than an increase in dues charged to members. Indeed, if the club could be made self-sustaining by grazing fees, guest fees and other prerequisites, its operations being for the stated purposes, its exempt status would not be affected. We need but to extend this principle to the acquisition of the preserves themselves to demonstrate that the granting of oil leases to obtain money with which to pay the mortgage debt did not change the character of the organization.”

Exhibit No. 2—(Continued.)

* * * *

“We think the question is controlled by the decision in Trinidad v. Sagrada Orden, 263 U.S. 578, 44 S. Ct. 204, 68 L. Ed. 458, wherein the court points out that the statute says nothing about the source of the income, but makes its destination the ultimate tests of exemption. The act here involved provides [27] exemption for ‘clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings or which inures to the benefit of any private shareholder,’ while the statute before the Supreme Court provided exemption for corporations ‘organized and operated exclusively for religious, charitable, scientific or educational purposes, no part of the net earnings of which inures to the benefit of any private stockholder or individual.’ The necessity of having money to carry on the enterprise, whether charitable or recreational, is present in both cases. Deriving funds from the properties owned to further either of these ends would be no more a departure in one case than in the other.”

(Emphasis supplied.)

Likewise, it was held in The Goldsby King Memorial Hospital, a Corporation, v. Commissioner, CCH. Dec. 14042 (M) that a corporation otherwise exempt is not deprived of exemption be-

Exhibit No. 2—(Continued.)

cause it incidentally carries on a profitable activity in furtherance of its predominant charitable purpose.

In *Anderson Club Inc., v. Commissioner of Internal Revenue*, 2 T.C. 1238, petitioner was incorporated under the Indiana Business Corporations Act in 1921 to act as the successor to an unincorporated association formed in 1902 for the purpose of constructing and operating a golf course and country club. The golf course and club house were located on a tract of land leased by the association. Upon the expiration of the lease the owners of the land demanded such an increase in rental upon renewal that it was decided to buy the land. It was necessary to buy the entire tract, including some acreage which proved to be unsuitable for a golf course. Petitioner's attempts to sell this unusable acreage as a whole being unsuccessful, it was sold over a period of years by small tracts at considerably in excess of cost. The profits on the sales amounted to about \$20,000 in two years, and all of such profit was required by the terms of the mortgage to be used, and was used, to reduce the mortgage and bonded indebtedness of the club. The club also conducted a "Winter Club" in downtown Anderson and profits of approximately \$3,000 were derived from this activity in the same two years. In [28] holding the club exempt under Section 101 (9), the Tax Court referred to the fact that the Commissioner's "regulations recognized the fact that an incidental sale of property does not extin-

Exhibit No. 2—(Continued.)

guish the right to exemption;" that "the fact that the profits were in some years substantial does not affect the incidental nature of the sales," and referred to *Koon Kreek Klub v. Thomas*, *supra*, and *Santee Club v. White*, 87 Fed. (2d) 5, where the incidental revenue under consideration was quite substantial, but in each of which cases, as stated by the Tax Court, the club was held to be exempt. The Court further held that the activities of the "Winter Club" were not such as to deprive petitioner of its exempt status.

It was also held in *Town and Country Club v. Commissioner*, (CCH Dec. 12924-A, December 30, 1942) where the petitioner purchased property to serve as a club house in downtown San Francisco, at 218 Stockton Street, and rented two stores on the ground floor, that such profit-making activities did not preclude the corporation from exemption under Section 101 (9) of the Code. In that case again reference was made to the *Trinidad v. Segrada* case, *supra*, decided by the Supreme Court of the United States, and it was pointed out that since that decision "it has been consistently held that it is not the source of the corporation's incidental profits that is controlling, but their destination which controls exemption from tax".

In *Roche's Beach, Inc., v. Commissioner of Internal Revenue*, 96 F. (2d) 776 the 2nd Circuit Court of Appeals held, with reference to a corporation organized for charitable purposes, that to come within the exemption, an otherwise exempt corporation is not precluded from engaging in busi-

Exhibit No. 2—(Continued.)

ness activities for profit, and that the destination, the exempt purpose, is more significant than the source of the income.

The First Circuit Court of Appeals also held in *Santee Club v. White*, 87 F. (2d) 5, above referred to, that profitable transactions [29] incidental to the main non-profitable purpose and activities of an organization do not affect the non-profitable character of the organization.

Again in *Schofield v. Corpus Christi Golf and Country Club*, 127 F. (2d) 452, the 5th Circuit Court of Appeals held the fact that the taxpayer, a golf and country club, had executed an oil lease on its property and received sums as royalties and bonus under the lease, did not preclude taxpayer from being a "club organized and operated exclusively for non-profitable purposes" within the terms of Sec. 101 of the Code, where the taxpayer's operations were the same before and after the lease and none of the net earnings inured to the benefit of any private shareholder. There the revenues from oil operations were quite substantial. The plaintiff leased property to the Taylor Refining Company for a cash bonus of \$7,500, an oil payment of \$60,000 out of a certain part of the oil, and a royalty in addition thereto. The Court there said:

"The statute expressly gives the exemption to clubs operated as this one was and as long as the exemption holds, all revenues of the club without regard to their source, are exempt from tax, because under the statute it is the nature and character of the operations of

Exhibit No. 2—(Continued.)

the club and the use made of the revenues, and not their source, which determines the exemptions. The judgment was right. It is affirmed.”

(Emphasis supplied.)

(C) No part of the Association's net earning inures to the benefit of any private shareholder.

No part of the Association's net earnings have ever been distributed to any of its members, and inasmuch as it has been held (see *Koon Kreek Klub v. Thomas et al.*, *supra*) that so long as profits “are retained by the organization or used to further the purposes which are made the basis of exemption and are not otherwise used for the benefit of any private shareholder * * *,” such profit cannot be deemed to inure to the benefit of any private shareholder, it follows that, under the facts stated, no part of this Association's net [30] earnings inures to the benefit of any private shareholder.”

(D) California State Automobile Association Inter-Insurance Bureau.

The California State Automobile Association Inter-Insurance Bureau is not a part or a subsidiary of the California State Automobile Association, but is an entirely separate and distinct organization and entity. This Bureau was formed and is operated, in their own particular behalf, by a group of Association members for the purpose of providing indemnity among themselves, i.e., the subscribers to the Bureau, who desire to protect themselves against various automobile hazards, the exchange of indemnity being effected by an agent holding

Exhibit No. 2—(Continued.)

a power of attorney for that purpose from each individual in the group.

The Association and the Bureau, each with its own staff of employees, occupy common quarters and share the expense of same. They also share certain other expenses when, for convenience, an employee of one organization also performs services for the other. It cannot be too strongly emphasized, however, that neither organization derives any profit from the operation of the other.

The Inter-Insurance Bureau is itself a non-profit concern. Its funds, consisting of the accumulated premium deposits of its subscribers belong solely to them, and interest earned thereon accrues to their several accounts.

A special accident policy written and issued exclusively for members of the Automobile Association with the North American Insurance Company is issued to such members, and the premiums on said policies are paid out of membership dues; and to further assist the members in obtaining reliable insurance coverage on their automobiles, the Association has arrangements with the Inter-Insurance [31] Bureau, which Insurance Bureau under its rules and regulations writes insurance only for those members of the Automobile Association who desire it. At the present time, approximately 65% of the members of the Association carry insurance with the Bureau, but it should be emphasized that no member is required to insure with the Bureau, and any member may insure with any insurance company of his own choice.

Exhibit No. 2—(Continued.)

About two-thirds of the members of the Automobile Association have chosen to become subscribers to the Bureau by insuring with it, but the remaining members of the Association prefer to obtain their automobile insurance from other reciprocal, mutual, or stock insurance companies. It should also be pointed out that the premiums or rates charged to policy holders of the Inter-Insurance Bureau are the same as those charged by what are known as the Board or Conference companies, they being the standard rates which are of course, higher than those of many of the independent companies but are lower than none, so that those members of the Association who are also subscribers to the Bureau do not obtain any discount on insurance rates. Being a reciprocal company, it is the practice to pay back to policy holders after the expiration dates of the respective policies, a proportionate share of any savings which may be obtained during that policy year. However, this is the customary practice followed by all reciprocal or mutual insurance companies, and no unusual benefits are therefore derived by members who take out their policies with the Inter-Insurance Bureau.

(E) The California State Automobile Association is different in many essential respects from the M Association described in G.C.M. No. 23688.

This Association is wholly unlike the Automobile Association dealt [32] with in G.C.M. 23688, which is stated to function as a federation of automobile clubs and a managing agency of several local auto-

Exhibit No. 2—(Continued.)

mobile clubs. This Association does not conduct or participate in any such functions, nor does it organize, supervise, or grant affiliation to other corporations, associations, or organizations with similar objects and purposes, as described in (f) of the by-laws of M Association. It has no member clubs and has never been operated as a federation of automobile clubs.

It is sharply distinguished from the M Association also in that members may not purchase insurance "at a considerable saving in premiums", nor does it bear any resemblance whatsoever to the organization described in G.C.M. 23688 whereby "Arrangements have also been made with certain merchants in one area whereby members of one of the local organizations may purchase clothing, laundry, furniture, and automobile supplies at less than the usual selling prices of such articles."

Another difference between this Association and the M Association is that in the latter, individual members as such have no right to vote or participate in the affairs of the corporation, whereas in our Association the individuals have both of such rights, and do actively participate in the affairs of the corporation. Likewise, our Association, unlike the M Association, does consist of members who participate in activities leading to the rendition of the services previously herein enumerated, all of which are designed to and do contribute to the pleasure and recreation of the membership.

Again, there is a radical difference between the M Association, which is stated in G.C.M. 23688

Exhibit No. 2—(Continued.)

to operate "in the nature of a non-profit cooperative buying association," as the California State Automobile Association indulges in no such activities whatever. Members of this Association [33] are not able, as the members of the M Association are, to make certain purchases at less than market price, nor are they able to obtain insurance coverage at reduced premium costs.

A comparison of the activities of our Association show it to be widely divergent from the M Association in practically every respect. [34]

CONCLUSION

It is respectfully submitted that under the definitions hereinabove cited, the Association is clearly a "club" within the purview of Section 101 (9), and that it is organized and operated exclusively for pleasure, recreation, and other non-profitable purposes. It is unquestionably true that the members of this Association are banded together to enjoy the benefits resulting from the collective action of the large membership in constantly extending and improving motoring conditions throughout the northern part of California, and furnishing its members information and advice concerning such conditions, and that this, contrary to the statement made in the Commissioner's letter of September 23, 1944, *supra*, is the common objective of the Association in which all members participate. The Association is in no sense whatever a cooperative, was not organized and is not operated as a cooperative, and furnishes none of the discounts and sav-

Exhibit No. 2—(Continued.)

ings which are customarily available to members of a cooperative.

The primary rule in the construction of a statute is to ascertain and give effect to legislative intention. *Fidelity and Deposit Co. of Maryland v. Arenz*, 290 U. S. 66. And, in ascertaining and giving effect to such intention, the words used in the statute are to be given their common, ordinary meaning in the absence of contrary indication either in the statute or surrounding circumstances. *Van Weise v. Commissioner of Internal Revenue*, 69 Fed. (2d) 439 cert. den. 54 S. Ct. 866, 292 U. S. 655.

A very exhaustive search and study of relevant cases, including those cited in *Arner v. Rogan*, *supra*, has failed to reveal a single decision which might be construed as holding that a "club" in the general sense and distinguished from clubs which have a social, athletic, or sporting purpose, contemplates the commingling of members in fellowship. [35]

As previously pointed out, Section 101 (9) makes no mention whatever of social, athletic, or sporting activities, and the innate characteristic of social, athletic or sporting clubs must not be confused with the characteristics inherent in clubs generally. Clubs may have an infinite variety of purposes, none of which contemplate a commingling of their members. The characteristic common to all clubs, properly so-called, is the association of individuals to reach a common objective, and it is this char-

Exhibit No. 2—(Continued.)

acteristic which controls the proper meaning of the term “club” and gives it its generally accepted meaning, to wit, an association of individuals who “combine for the promotion of some common object”. It is this common, ordinary meaning which should be applied in the interpretation of Section 101 (9).

It seems inescapable, therefore, that this Association must be held to be a club within the purview of Section 101 (9). The Association is composed of individuals who are associated together for the furtherance of pleasure and recreation through motoring. Commingling of persons is not inherent or necessary to pleasure and recreation (see *supra*) and the members give effect to their association through the Board of Directors elected by them, and through the numerous committees hereinbefore enumerated which carry on the affairs of the Association for the common good of all the members. It would be difficult to find a more outstanding example of an association for the achievement of a common purpose, in order to illustrate the proper definition of the word “club” in its generally accepted sense.

With regard to the contention in the Commissioner’s letter of September 23, 1944, that the Association’s principal activity is the “rendering to members upon payment of an annual fee, services of the type available to motorists generally on a commercial scale at greater cost,” it cannot be too strongly emphasized that such contention utterly

Exhibit No. 2—(Continued.)

disregards the purpose [36] for which the Association is organized and operated, and upon which exemption is predicated. The sole purpose for which the Association is organized and operated is the pleasure and recreation of its members and other non-profitable purposes, and it cannot be gainsaid that the provision by the Association for emergency road service, lists of accredited garages, hotels and other stopping places for the comfort and convenience of its members, furnishing maps, routings and general motoring information, all directly contribute to their pleasure and recreation. All the Association's activities are incidental to this sole purpose and are engaged in with but one end in view, namely, the achievement of said purpose. The Association is neither organized nor operated for the purpose of rendering services of a commercial nature to its members, and the great majority of such services are not obtainable commercially at greater cost or at any cost. There is no commercial organization qualified or equipped to furnish touring information and comparable advice to motorists, at least in the section served by this Association, so that the services primarily desired by motorists in such section cannot be obtained from any commercial organization.

As previously pointed out the Association can in no way be compared to a non-profit cooperative buying association, which is organized and operated for the purpose of rendering services of a commercial nature to its members, with attendant discounts or savings in costs.

Exhibit No. 2—(Continued.)

The activities of the Touring Bureau of the Association reflect most graphically the use made by the Association's membership of the facilities set up for their pleasure and recreation, which is its primary function.

The following excerpt from the Report of the President of the Association for 1940, in which year pleasure and recreational trips were [37] still on practically a normal basis, is highly illustrative:

“The record-breaking flow of motor travel in California and throughout the entire west last year was strongly reflected in activities of your Association's Touring Bureau, Volume of service again demonstrated that the bureau is most widely used of any agency in the entire west for the guidance and planning of motor tours. During the year Touring Bureau staffs in Association offices personally served 199,126 motor touring parties, including members of affiliated A.A.A. clubs who came in record numbers to visit the Exposition and tour California, other western states, and western Canada. The bureau prepared 19,112 transcontinental routings, and 30,256 other out-of-state routings. Road maps issued totalled 367,270. In addition to these personally rendered services, the bureau handled 170,201 telephoned requests from members seeking travel information, exclusive of thousands of such inquiries received by San Francisco headquarters and

Exhibit No. 2—(Continued.)

not tabulated. The Bureau issued 24,870 tourist court and cabin lists and 44,000 monthly hotel and resort lists. Foreign travel was affected by conditions abroad, yet the bureau handled shipment of 35 cars for members making European tours and arranged for driving licenses and other documents.”

The real purpose for which the Association is organized and operated should therefore control, in conformity with the provisions of Section 101 (9). And inasmuch as the sole purpose for which the Association is organized and operated falls squarely within the said subsection, we respectfully submit that the Association is entitled to exemption from Federal income tax as “a club organized and operated exclusively for pleasure, recreation and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.”

It is believed that all the conditions of the statute have been met by this Association, which may be unique in that respect, and that it is entitled to the restoration of its tax exempt status effective as of January 1, 1943. [38]

II.

As stated on a rider attached to the corporation income tax return for the calendar year 1943, and an identical rider attached to the corporation excess profits tax return for the calendar year 1943, which returns were filed by the Association with the Collector of Internal Revenue at San Francisco

Exhibit No. 2—(Continued.)

on September 14, 1945, the preparation and filing of the said returns resulted from instructions received from the Commissioner of Internal Revenue in his letter dated July 27, 1945, and that the filing of said returns and the payment of the taxes shown thereon were made under protest as the taxpayer believes it is rightfully entitled to tax exemption. On the aforesaid date of filing said returns, taxpayer paid income taxes for 1943 in the amount of \$27,633.38 and on October 23, 1945, interest in the amount of \$2,485.11, making a total of \$30,118.49 and on September 14, 1945, the claimant paid excess profits taxes in the amount of \$129,178.22 and on October 23, 1945, interest of \$11,617.19 making a total of \$140,795.41.

III.

Claimant respectfully requests and demands that the sum of \$27,633.38, representing income taxes together with interest thereon in the amount of \$2,485.11 paid for the calendar year 1943 be refunded together with interest as provided by law, for the reasons hereinabove set forth. Coincident with the filing of this Claim for Refund, a similar request and demand is being made for the refund of excess profits taxes in the amount of \$129,178.22, together with interest thereon in the amount of \$11,617.19.

IV.

Claimant requests and demands such further or additional refund or [39] refunds as may now or hereafter appear to be due it by reason of the fore-

Exhibit No. 2—(Continued.)

going or on account of (a) any mistake in fact or in law made by it or any officer, clerk or other employee of the Treasury Department in the preparation, amendment and/or adjustment of the said return, (b) any mistake in the payment and/or collection of the tax made by any person designated in subdivision (a) of this paragraph, (c) any erroneous or illegal requirement or regulation of any officer, clerk or other employee of the Treasury Department, (d) any repealed law, whether heretofore or hereafter repealed, (e) any unconstitutional law, whether heretofore or hereafter declared unconstitutional, or (f) any other act or matter in connection with the said return, whether covered by the foregoing or not so covered. [40]

EXHIBIT No. 3

Form 843, Treasury Department, Internal Revenue Service, (Revised April 1940)

CLAIM

To Be Filed With the Collector Where Assessment
Was Made or Tax Paid

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[X] Refund of Tax Illegally Collected.

[] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

Exhibit No. 3—(Continued)

[] Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California,

City and County of San Francisco—ss.

Name of taxpayer or purchaser of stamps California State Automobile Association.

Business address 150 Van Ness Avenue, San Francisco 2, California.

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was led 1st California.

2. Period (if for income tax, make separate form for each taxable year) from January 1, 1943, to December 31, 1943.

3. Character of assessment or tax, excess profits tax.

4. Amount of assessment, \$140,795.41; date of payment, Sept. 14, 1945, \$129,178.22; Oct. 23, 1945, \$11,617.19.

5. Date stamps were purchased from the Government

6. Amount to be refunded, \$140,795.41.

7. Amount to be abated (not applicable to income or estate taxes)

8. The time within which this claim may be legally filed expires, under Section 322 IRC, on September 14, 1948.

Exhibit No. 3—(Continued)

The deponent verily believes that this claim should be allowed for the following reasons:

See Statement Attached.

/s/ CALIFORNIA STATE
AUTOMOBILE ASSN.,

By D. E. WATKINS,
Sec'y & Gen. Mgr.

Sworn to and subscribed before me this 23rd day
of October, 1945.

CON T. SHEA,

Notary Public in and for the City and County of
San Francisco, State of California. [41]

[Clerk's Note: Statement attached to Exhibit
No. 3 is identical with Exhibit No. 2 reproduced
at page 21, except for paragraphs II and III
appearing on pages 52 and 53. Paragraphs II
and III of Exhibit No. 3 are here set forth:]

II.

As stated on a rider attached to the corporation
income tax return for the calendar year 1943, and
an identical rider attached to the corporation ex-
cess profits tax return for the calendar year 1943,
which returns were filed by the Association with
the Collector of Internal Revenue at San Francis-
co on September 14, 1945 the preparation and filing
of the said returns resulted from instructions re-
ceived from the Commissioner of Internal Revenue
in his letter dated July 27, 1945, and that the filing
of said returns and the payment of the taxes there-
on were made under protest as the taxpayer be-
lieves it is rightfully entitled to tax exemption. On

Exhibit No. 3—(Continued)

the aforesaid date of filing said returns taxpayer paid income taxes for 1943 in the amount of \$27,633.38 and on October 23, 1945 interest in the amount of \$2,485.11 making a total of \$30,118.49 and on September 14, 1945 the claimant paid excess profits taxes in the amount of \$129,178.22 and on October 23, 1945 interest of \$11,617.19 making a total of \$140,795.41.

III.

Claimant respectfully requests and demands that the sum of \$129,178.22, representing excess profits taxes together with interest thereon in the amount of \$11,617.19 paid for the calendar year 1943 be refunded together with interest as provided by law, for the reasons hereinabove set forth. Coincident with the filing of this Claim for Refund a similar request and demand is being made for the refund of income taxes in the amount of \$27,633.38 together with interest thereon in the amount of \$2,485.11.

* * * *

[66]

EXHIBIT No. 4

Form 843, Treasury Department, Internal Revenue Service, (Revised April 1940).

Copy

CLAIM

To Be Filed With the Collector Where
Assessment Was Made or Tax Paid

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[X] Refund of Tax Illegally Collected.

[] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

[] Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California,

City and County of San Francisco—ss.

Name of taxpayer or purchaser of stamps, California State Automobile Association.

Business address, 150 Van Ness Avenue, San Francisco 2, California.

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed, 1st California.

2. Period (if for income tax, make separate form for each taxable year) from January 1, 1944, to December 31, 1944.

3. Character of assessment or tax, Income Tax.

4. Amount of assessment, \$37,947.20; dates of payment, Sept. 14, 1945, \$36,844.39; Oct. 23, 1945, \$1,102.81.

5. Date stamps were purchased from the Government

6. Amount to be refunded, \$37,947.20.

7. Amount to be abated (not applicable to income or estate taxes)

8. The time within which this claim may be

legally filed expires, under Section 322 IRC, on Sept. 14, 1948.

The deponent verily believes that this claim should be allowed for the following reasons:

See Statement Attached.

/s/ CALIFORNIA STATE
AUTOMOBILE ASSN.,
By D. E. WATKINS,
Sec'y. & Gen. Mgr.

Sworn to and subscribed before me this 23rd day of October, 1945.

CON T. SHEA,
Notary Public in and for the City and County of
San Francisco, State of California. [68]

[Clerk's Note: Statement attached to Exhibit No. 4 is identical with Exhibit No. 2 reproduced at page 21, except for paragraphs II and III appearing on pages 52 and 53. Paragraphs II and III of Exhibit No. 4 are here set forth:]

II.

As stated on a rider attached to the corporation income tax return for the calendar year 1944, and an identical rider attached to the corporation excess profits tax return for the calendar year 1944, which returns were filed by the Association with the Collector of Internal Revenue at San Francisco on September 14, 1945, the preparation and filing of said returns resulted from instructions received from the Commissioner of Internal Revenue in his letter dated July 27, 1945, and that the filing of said returns and the payment of the taxes shown thereon were made under protest as the taxpayer

believes it is rightfully entitled to **tax exemption**. On the aforesaid date of filing said returns, taxpayer paid income taxes for 1944 in the amount of \$36,844.39 and on October 23, 1945 interest in the amount of \$1,102.81, making a total of \$37,947.20 and on September 14, 1945 the claimant paid excess profits taxes in the amount of \$23,306.42 and on October 23, 1945 interest of \$697.60 making a total of \$24,004.02.

III.

Claimant respectfully requests and demands that the sum of \$36,844.39, representing income taxes, together with interest thereon in the amount of \$1,102.81 paid for the calendar year 1944 be refunded together with interest as provided by law, for the reasons hereinabove set forth. Coincident with the filing of this Claim for Refund a similar request and demand is being made for the refund of Excess Profits Taxes in the amount of \$23,306.42, together with interest thereon in the amount of \$697.60.

* * * *

[94]

EXHIBIT No. 5

Form 843, Treasury Department, Internal Revenue Service, (Revised Jan. 1946).

Copy

CLAIM

To Be Filed With the Collector Where
Assessment Was Made or Tax Paid

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[X] Refund or Tax Illegally Collected.

[] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

[] Abatement of Tax Assessed (not applicable to estate, gift, or income taxes).

State of California,

City and County of San Francisco—ss.

Name of taxpayer or purchaser of stamps, California State Automobile Association.

Business address, 150 Van Ness Avenue, San Francisco 2, California.

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed, 1st California.

2. Period (if for income tax, make separate form for each taxable year) from January 1, 1944 to December 31, 1944.

3. Character of assessment or tax, Excess-profits tax.

4. Amount of assessment, \$24,004.02; dates of payment, Sept. 14, 1945, \$23,306.42; Oct. 23, 1945, \$697.60.

5. Date stamps were purchased from the Government

6. Amount to be refunded, \$24,004.02.

7. Amount to be abated (not applicable to income, gift, or estate taxes)

8. The time within which this claim may be legally filed expires, under section 322 IRC on September 14, 1948.

The deponent verily believes that this claim should be allowed for the following reasons:

See Statement Attached.

CALIFORNIA STATE
AUTOMOBILE ASSN.,

/s/ By D. E. WATKINS,
Sec'y. & Gen. Mgr.

Sworn and subscribed to before me this 23rd day of October, 1945.

CON T. SHEA,

Notary Public in and for the City and County of San Francisco, State of California. [96]

[Clerk's Note: Statement attached to Exhibit No. 4 is identical with Exhibit No. 2 reproduced at page 21, except for paragraphs II and III appearing on pages 52 and 53. Paragraphs II and III of Exhibit No. 5 are here set forth:]

II.

As stated on a rider attached to the corporation income tax return for the calendar year 1944, and an identical rider attached to the corporation excess profits tax return for the calendar year 1944, which returns were filed by the Association with the Collector of Internal Revenue at San Francisco on September 14, 1945, the preparation and filing of said returns resulted from instructions received from the Commissioner of Internal Revenue in his letter dated July 27, 1945, and that the filing of said returns and the payment of the taxes shown

thereon were made under protest as the taxpayer believes it is rightfully entitled to tax exemption. On the aforesaid date of filing said returns, taxpayer paid income taxes for 1944 in the amount of \$36,844.39 and on October 23, 1945, interest in the amount of \$1,102.81, making a total of \$37,947.20, and on September 14, 1945, the claimant paid excess profits taxes in the amount of \$23,306.42 and on October 23, 1945, interest of \$697.60, making a total of \$24,004.02.

III.

Claimant respectfully requests and demands that the sum of \$23,306.52, representing excess profits taxes, together with interest thereon in the amount of \$697.60 paid for the calendar year 1944, be refunded, together with interest as provided by law, for the reasons hereinabove set forth. Coincident with the filing of this Claim for Refund, a similar request and demand is being made for the refund of income taxes in the amount of \$36,844.39, together with interest thereon in the amount of \$1,102.81.

* * * *

[122]

[Endorsed]: Filed May 26, 1948.

[123]

[Title of District Court and Cause.]

ANSWER

Defendant answers as follows:

I.

Admits the allegations contained in paragraph I of plaintiff's complaint.

II.

Admits the allegations contained in paragraph II of plaintiff's complaint.

III.

Admits the allegations contained in paragraph III of plaintiff's complaint.

IV.

Admits the allegations contained in paragraph IV of plaintiff's complaint.

V.

Admits the allegations contained in paragraph V of plaintiff's complaint, except denies that the taxes were paid on September 14, 1945, and avers that the taxes were paid on October 15, 1945, [124]

VI.

Defendant admits that the taxes of \$27,633.38 were paid but denies that the taxes were paid on September 14, 1945, and avers that the taxes were paid on October 15, 1945; admits that interest of \$2,485.11 was paid on October 23, 1945; denies that the taxes and interest, or any part thereof, were illegally collected and denies that any part thereof is due and owing to the plaintiff. Defendant avers that he is without knowledge or information sufficient to form a belief as to the truth of the remaining allegation contained in paragraph VI of plaintiff's complaint.

VII.

Denies all the allegations contained in paragraph VII of plaintiff's complaint, except admits that Section 101 (9) of the Internal Revenue Code contains the provisions alleged.

VIII.

Denies all the allegations contained in paragraph VIII of plaintiff's complaint.

IX.

Answering paragraph IX of the complaint defendant alleges that he is without knowledge or information sufficient to form a belief as to the truth of the allegations therein contained.

X.

Answering paragraph X of the complaint defendant alleges that he is without knowledge or information sufficient to form a belief as to the truth of the allegations therein contained.

XI.

Denies all the allegations contained in paragraph XI of plaintiff's complaint.

XII.

Admits the allegations contained in paragraph XII of plaintiff's complaint, except denies that any portion of the taxes or [125] interest was erroneously or illegally collected.

XIII.

Denies all the allegations contained in paragraph XIII of plaintiff's complaint.

XIV.

The allegations of paragraph XIV are admitted, except insofar as denied in paragraph V of this answer.

XV.

All of the allegations contained in paragraph XV of the complaint are denied, except as heretofore admitted. Defendant admits that interest of \$11,-617.19 was paid on October 23, 1945.

XVI.

Admits the allegations contained in paragraph XVI of plaintiff's complaint, except denies that the taxes and interest, or any portion thereof, were erroneously or illegally collected.

XVII.

Denies all the allegations contained in paragraph XVII of plaintiff's complaint.

XVIII.

Admits the allegations contained in paragraph XVIII of plaintiff's complaint, except insofar as denied in paragraph V of this answer.

XIX.

Denies all the allegations contained in paragraph XIX of plaintiff's complaint, except as heretofore admitted. Defendant admits that interest in the sum of \$1,102.81 was paid on October 23, 1945.

XX.

Admits the allegations contained in paragraph XX of plaintiff's complaint, except denies that the taxes or interest, or any part thereof, were erroneously or illegally collected. [126]

XXI.

Denies all the allegations contained in paragraph XXI of plaintiff's complaint.

XXII.

Admits the allegations contained in paragraph XXII of plaintiff's complaint, except as denied in paragraph V of this answer.

XXIII.

Denies all the allegations contained in paragraph XXIII of plaintiff's complaint, except as hereto-

fore admitted. Defendant admits that interest in the sum of \$697.60 was paid on October 23, 1945.

XXIV.

Admits the allegations contained in paragraph XXIV of plaintiff's complaint, except denies that the taxes or interest, or any part thereof, were erroneously or illegally collected.

XXV.

Denies all the allegations contained in paragraph XXV of plaintiff's complaint.

Wherefore, having fully answered, defendant prays judgment and costs.

FRANK J. HENNESSY,
United States Attorney.

/s/ WILLIAM E. LICKING,
Asst. United States Attorney,
Attorneys for Defendant.

[Endorsed]: Filed July 26, 1948.

[127]

[Title of District Court and Cause.]

OPINION AND ORDER

Plaintiff is a non-profit, non-stock corporation, organized in the year 1907 under the laws of the State of California. This action is brought to recover income and excess profit taxes, plus interest to the date of payment, assessed for the years 1943 and 1944, and interest on the aggregate amounts from the dates of the alleged overpayments.

The tax returns and the consequent payment of

taxes for these years were made as the result of a demand by the Commissioner of Internal Revenue. The plaintiff had, prior to the years in question, been exempt from the payment of income and excess profit taxes.

The membership of the plaintiff corporation is largely made up of owners of pleasure cars. There is rendered to the members towing service, emergency road service, touring bureau service and service on the procuring of motor licenses. Plaintiff has rendered service to the public generally through road signing and [128] various war services in connection with the problems arising during the gas rationing period, acting as an official agency for the Federal Government in signing of highways in dim-out and black-out areas, and in rendering to members of the armed forces its services without cost. The taxpayer publishes a monthly magazine known as the "Motor Land". During the years in question it had no income from advertising. It was distributed to the entire membership and was not sold generally to the public. The emergency road service afforded the members is rendered under contracts which plaintiff makes with garages. This service is restricted to passenger cars. The garage bills are paid for by the members who receive the service but plaintiff makes no charge to the members for towing service. If a member is involved in an accident, plaintiff undertakes to adjust the matter of damages, and, if the member is involved in an arrest in a remote place, counsel is provided by the associa-

tion; if a fine is assessed the fine is paid by the plaintiff and the member is called upon to reimburse plaintiff for such outlay. The legal service which is rendered is furnished pursuant to an agreement made by the plaintiff and the State Bar of California. Plaintiff gives to its members a special limited traffic accident policy written by the North American Accident Insurance Company. The California State Automobile Inter-Insurance Bureau affords insurance service to certain of plaintiff's members. The bureau is a separate corporate entity. It is a reciprocal insurance exchange for the inter-exchange of insurance on a cooperative basis. No one can be so insured unless he is a member of the plaintiff association. The insurance is restricted to certain individuals who meet certain qualifications. There is no requirement that a member of the [129] plaintiff association become a subscriber to the bureau. The bureau writes participating insurance. The plaintiff and the bureau occupy the same office quarters in San Francisco and in each of thirty-five district offices. The bureau compensates the plaintiff for the space it occupies, the rental being calculated on a square foot basis. Other expenses, including personnel costs, are divided upon the basis of proper percentage of costs that should be borne by each organization and no profit was derived by plaintiff through its relationship with the bureau. Dues for the years in question were \$12 per year, plus an initiation fee for \$3 for the first year. Membership is open to all owners of automobiles who are not considered

too old and who are deemed to be persons without a bad traffic record or otherwise irresponsible. No social, racial or religious discrimination is made with reference to membership. It has been the policy of plaintiff to expend its annual income for services but during the years 1943 and 1944 for reasons readily apparent its services were restricted and curtailed. No dividends have been declared by plaintiff to its members and its income has never been paid or credited on its books to any of its members. The directors of the association serve without financial remuneration. The members have the right to participate in the affairs of the plaintiff, including their presence at the annual board meetings, notices of which are sent out at least 60 days prior to the meeting. Although plaintiff has no member clubs it is affiliated with the American Automobile Association and under that affiliation plaintiff recognizes the membership of such other clubs affiliated with that association when such members are visiting plaintiff's territory and such [130] visitors are entitled to many of the services above enumerated. Outside of the annual meeting, the meetings of the Board of Directors and other meetings occasionally called by plaintiff and its committees (which the members are entitled to attend), plaintiff does not have any social features. There are other activities such as safety education work, the distribution of safety posters and the sponsoring of school safety patrols, the making of traffic surveys and participation in activities relating to vehicle legislation, in which the plaintiff en-

gages. Plaintiff's records show that on December 31, 1937, there was a slight excess of receipts over expenditures but that during each of the years 1938, 1939 and 1940 there was a deficiency; that during the next 5 years the income exceeded the expenses and this resulted in surplus balances for each of these years. In 1946 the expenditures exceeded the income. A check of 16 years shows a surplus for 8 years and a deficiency for 8 years.

This abridged recital of the purposes and activities of plaintiff corporation is sufficient as a basis for approaching the problem which is to be solved, whether plaintiff comes within the exemption which excludes from the tax organizations falling within Section 101 (9) of the Internal Revenue Code, which reads as follows:

“Clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.”

This section poses three questions. 1. Is the plaintiff a club? 2. Is plaintiff organized and operated exclusively for pleasure, recreation and other non-profitable purposes? 3. Do any of its net earnings inure to the benefit of any of its members?

The New International Encyclopedia defines “club” [131] as “A word said to be derived from the Saxon cleafan to divide—a club being an association the expenses of which are shared among its members.” It “indicates a division of the reckoning”, *Merion Cricket Club v. United States*, 119

F. 2d 578, "a definite association organized for indefinite existence; not an ephemeral meeting for a particular occasion to be lost in a crowd at its dissolution", *Eichbaum v. Irons*, 6 Watts & S. 67. Plaintiff is an association the expenses of which are shared among its members. Equivalence between the proportion of a member's contributions and the benefits which he enjoys is of no moment as long as there is payment by him for the repeated use of its facilities, available to the members. The services provided by plaintiff to its members are for their pleasure and recreation, to enjoy to the extent the wants or fancies of the individual member requires.

Defendant contends that in order to constitute a club the purposes and activities must embrace a commingling of the members, one with the other, in fellowship; that it is not sufficient that the members make a common cause in a financial or other sense or that there be present group activity, both of which conditions are here found. *United States v. Anderson*, 108 F. 2d 475 and *Arner v. Rogan*, 27 A.F.T.R. 1093, cases in which the application of the excise tax under Section 501 of the Revenue Act of 1926 on "any amount paid * * * as dues or membership fees to any social, athletic or sporting club or organization" are advanced by defendant in support of its position. This section imposes an excise tax upon membership fees or dues while section 101 (9) exempts from income tax associations coming within the description. In considering the two statutes there is wanting identity in

objectives. There is differentiation [132] also in the terms used. A "social club" has a meaning different from a club "organized and operated exclusively for pleasure or recreation purposes." Webster defines the adjective "social" as "That is spent, taken, enjoyed, etc., in the company of one's friends or equals; as agreeable social relations." To be classed as a social club under the taxing statute the predominant purpose of the taxpayer must be social, (*Tidwell v. Anderson*, 4 F. Supp. 789). If it has some social activities this alone does not make it a social club and it is not such if the social features are merely incidental to main purposes which are of a nature other than social, *Bankers' Club of America v. U. S.* 37 F. 2d 982, or at least the social features must be a material part, *Merchants Club v. U. S.* 66 F. Supp. 126. The generic term "club" is used in both statutes; this alone is common to the two. The adjective "social" qualifies the noun "club" and limits it to such organizations as are "social" as above defined. It appears clear that a club operated for pleasure or recreation is one in which the members may carry out or enjoy those purposes acting either individually or collectively. It would require a strained and unwarranted construction to read into the description the qualification of "social". Had Congress so intended, such intention could readily have been expressed by supplying the adjective "social" as it did in section 501.

Is plaintiff organized and operated exclusively for pleasure, recreation and other non-profitable purposes?

The Collector says that if there exists a single purpose which is neither, pleasure, recreation or non-profitable, plaintiff may not be said to come within the exemption, and that this follows regardless of the number [133] and importance of the purposes falling within the designated purposes. *Better Business Bureau v. United States*, 326 U. S. 279, cited in support, would apply, (as that case limits itself), only if the other purposes are "substantial in nature". This theme is in Treasury Regulation 111 which deals with Section 101 (9), "Generally, an incidental sale of property will not deprive the club of the exemption". If the income is applied in carrying out the non-profitable purpose the exemption applies and this results without regard to the source of the income. *Scofield v. Corpus Christi Golf & Country Club*, 127 F. 2d 452. This is the line in the cases cited which bear upon the subject. But, it is replied, towing automobiles to garages, making emergency repairs, adjusting claims, pleading in traffic violation cases and payment of fines, supplying accident policies, renewing licenses and attending to the details of transfer of title to automobiles, services afforded through contracts with garages, lawyers, and insurance companies, do not come within the restricted meaning of "pleasure" and "recreation". The sum of the picture must be appraised. All of this was designed primarily to alleviate the hardships and inconveniences which sometimes arise in pleasure driving. It is reasonable to conclude that these services are within the listed purposes. Dur-

ing the years in question gasoline rationing was in effect. The basic "A" Book entitled a holder to gasoline which permitted him to drive his automobile about ninety miles per month. This, it is assumed, was used in obtaining the necessities of life for himself and family. Supplemental ration was required to be used for essential occupational purposes. Defendant Collector concludes that it is questionable whether any material part of plaintiff's activity during these years had to do with the pleasure or recreation [134] of its members. Plaintiff replies that the income, other than from membership dues and fees and reimbursements of charges advanced for the account of members, are insignificant in amount and not "substantial"; that the excess of income over expenditures were not profits and that no activities were conducted with third parties with the purpose of creating profits. I agree with plaintiff. The largest item of expenditure appears to be for the maintenance and operation of thirty-four branch offices maintained by plaintiff for the purpose of affording the members the services outlined. Included therein is reimbursement by the Bureau, computed on a cost basis. The next largest item of expenditure covers the emergency road service. No element of profit enters into that service. The other items of expenditures relate to services rendered the members and do not embrace financial profit. The argument is not persuasive that because the income exceeded the expenditures in each of these two years the purposes are not non-profitable. It is explained in

the evidence that this net income resulted from a curtailment of services during war conditions due to restrictions in pleasure driving. It has never been the intent of the plaintiff to build up a surplus, or to gain a profit, for itself or its members. The record discloses that the excess of membership dues and fees over expenditures in these years is offset by the cost of services to members in other years. The purpose of profit is not discoverable in the facts. The distinction is in the purpose. Or as the Supreme Court stated in *Trinidad v. Sagrada*, 263 U. S. 578, dealing with a similar exemption, "says nothing about the source of the income, but makes the destination the ultimate test of exemption". [135]

Though the services may have been rendered to many members who availed themselves thereof in their businesses rather than for pleasure or recreation this would not require the conclusion that the purposes are not within the exemption. The main objective is not financial gain to members but the rendering to them services which lend to their convenience in non-business activities. Membership in most organizations which are characteristically non-profitable has some element of commercialism. Since plaintiff's objectives translated into its activities are essentially non-profitable in a commercial sense, either to itself or to its members, it would appear that plaintiff is engaged in a non-profitable undertaking.

There is here not present the conducting of a "substantial and profitable business * * * which

had only an indirect relation to the original purpose for which it was created", as was apparent in *Aviation Club of Utah v. Commissioner*, 7 T.C. 366, affirmed in *Circuit Court of Appeals*, par. 72,-503 P.H. Federal Tax Service 1947, where the profits were derived from outside sources, "wholly disproportionate to its non-taxable purposes". The same differentiation must be kept in mind when considering such cases as *West Side Tennis Club v. Commissioner of Internal Revenue*, 111 F. 2d 6, where more than one-half of the club's income came from sales to the public of tickets to its tennis matches, or *Jockey Club v. Helvoring*, 76 F. 2d 598, where the income from transactions with outsiders was more than their cost to the club.

Finally, answer must be given to the claim that during these years 1943 and 1944 there accrued net earnings which inured to the benefit of the members. The members of the plaintiff corporations would be entitled to [136] a pro-rate distribution of its assets upon dissolution and a member is to be considered a "private shareholder". *West Side Tennis Club* 39 B.T.A. 149. As above noted it has never been the intention to distribute any net income direct to the members. There, of course, exists an indirect benefit through the disbursement in subsequent years of the surplus which is accumulated in any one year, thus increasing the services in such later years. But the purposes are not thereby changed. Had the savings resulted in reducing the dues, or liability therefor, this would not mean that they inure to the benefit of the mem-

bers within the ambit of the statute, if the earnings are used to further the purposes which are made the basis for the exemption. *Koon Kreek Klub v. Thomas*, 108 F. 2d 616. The Supreme Court in *Trinidad v. Sagrada*, 263 U. S. 578, construed an exemption of similar import and stated that the activities of the taxpayer could not be carried on without money and that making its properties productive to the end that the income is used for its purposes does not alter or enlarge those purposes. It is not the source but the destination of the income that governs. *Scofield v. Corpus Christi Golf & Country Club*, *supra*. At least this is so, unless the profits are wholly disproportionate to its non-taxable purposes, *Aviation Club of Utah v. Commissioner of Internal Revenue*, 162 F. 2d 984, or derived from the public, *West Side Tennis Club v. Commissioner of Internal Revenue*, 111 F. 2d 6.

It is my conclusion that plaintiff meets the conditions which entitled it to exemption. Findings will be prepared and submitted pursuant to the local rule.

Dated February 26th, 1947.

DAL M. LEMMON,

United States District Judge.

[Endorsed]: Filed Feb. 26, 1948.

Entered in Civil Docket 2/27/48.

[137]

District Court of the United States, Northern
District of California, Southern Division

At a Stated Term of the Southern Division of the United States District Court for the Northern District of California, held at the Court Room thereof, in the City and County of San Francisco, on Thursday, the 26th day of February, in the year of our Lord one thousand nine hundred and forty-eight.

Present: The Honorable Dal M. Lemmon, District Judge.

[Title of Cause.]

ORDER FOR JUDGMENT IN FAVOR OF
THE PLAINTIFF AND AGAINST THE
DEFENDANT

This case having been heretofore tried and submitted, being now fully considered, it is, in accordance with an opinion this day signed and filed, Ordered that judgment be entered herein in favor of the plaintiff and against the defendant in accordance with the prayer of the complaint, upon findings of fact and conclusions of law and judgment to be prepared by the attorneys for the plaintiff and submitted to the court pursuant to the local rule. [138]

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above-entitled cause came on regularly for trial on the 25th day of June, 1947 before the Court, sitting without a jury; Plaintiff appearing by its attorneys, Arthur H. Deibert and George E. Sandford, and the Defendant appearing by William E. Licking, Assistant United States Attorney for the Northern District of California; and evidence both oral and documentary having been received and the Court having fully considered the same, hereby makes the following special Findings of Fact.

FINDINGS OF FACT

I.

That Plaintiff is and at all times herein mentioned was, a corporation organized and existing under and by virtue of the laws of the State of California, duly qualified to [139] transact business therein and having its principal place of business and office at 150 Van Ness Avenue, San Francisco 2, California, and within the First Internal Revenue Collection District of said State of California.

II.

That Defendant, James G. Smyth, a resident of said Northern District of California, is now and was at all times since the 14th day of May, 1945, the duly appointed, qualified and acting Collector of Internal Revenue for the First Internal Reve-

nue Collection District of California, and was the person to whom the sums herein sought to be recovered were paid by the Plaintiff.

III.

That Plaintiff at all times since the inception of Federal income taxation in 1913 had been exempt from the imposition of any Federal income and/or excess profits tax until it was finally advised by the Commissioner of Internal Revenue in a letter dated July 27, 1945, that further exemption was denied.

IV.

That because of said ruling of July 27, 1945 by the Commissioner of Internal Revenue the Plaintiff paid, under protest, income and excess profits taxes and interest thereon in the amounts and on the dates as follows:

1943—Income Tax and Interest.....	\$ 30,118.49
September 15, 1945	
1943—Excess Profits Tax & Interest..	140,795.41
September 15, 1945	
1944—Income Tax and Interest.....	37,947.20
September 15, 1945	
1944—Excess Profits Tax & Interest...	24,004.02
September 15, 1945	

Total.....	\$232,865.12
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V.

That the Plaintiff on or about October 23, 1945, and within two years of the payment of the amounts listed in paragraph IV above, filed claims for refund of said amounts respectively. Said claims set forth under oath the grounds for refund

relied upon by the Plaintiff and set forth sufficient facts to apprise the Defendant and the Commissioner of Internal Revenue of the exact basis of the said claims. The Commissioner of Internal Revenue rendered no decision on said claims within six months after the filing thereof, and the Plaintiff thereupon filed this action on May 29, 1946.

VI.

That the Plaintiff was organized in 1907 under the laws of the State of California as a non-profit corporation without capital stock. Each member possessed only one vote on the matters requiring action or sanction of the membership.

VII.

That the purposes of the Plaintiff have been practically unchanged since its organization and at all times pertinent herein were substantially as follows: to promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users; to urge adoption of just and intelligent legislation on the use of highways and the regulation of traffic thereon; to maintain offices for collecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles; to protect the legitimate interests of its members in connection with its purposes; to affiliate and associate with similar organizations. None of the foregoing or any other purposes of Plaintiff were designed or intended to make a profit. [141]

VIII.

That the Plaintiff has only the powers necessary to carry out its purposes. The Plaintiff has no power to distribute or set aside any portion of its net income to its members or to any other person except to carry out its purposes.

IX.

That in furtherance of the purposes for which it was originally organized as an automobile club, Plaintiff has provided during the years 1943 and 1944 as well as prior and subsequent to said years, (1) a Touring Bureau which provides the members with complete touring data and assists them in planning motor trips; (2) an Emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter automobile trouble on the highways, which service is restricted to passenger cars; (3) a Road Sign Department, which operates in conjunction with state and local authorities a service consisting of the erection and maintenance of direction and warning signs and historical markers; (4) a Public Safety Department, which carries on an active and aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions; (5) an Adjustment and Traffic Department, which advises and assists the members with respect to traffic violations and accidents; (6) a License Department, which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtaining automobile license

plates, as well as Federal auto tax stamps; and (7) a Magazine Department which publishes and distributes free to the members a magazine, keeping them informed of motoring conditions and improvements, and [142] specializing in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no paid advertising material since January 1, 1942. There is no sale or public distribution of said magazine.

X.

That the sum total of the activities of the Plaintiff is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by Plaintiff are for the pleasure and recreation of its members.

XI.

That in addition to the normal activities and services of the Plaintiff during the two years here in question, Plaintiff engaged in many activities incidental to the war effort and performed many services for the general public, such as road signing as an official agency of the Federal Government in blackout and dimout areas, services in connection with gas rationing, information and advice furnished members of the armed forces, training of drivers for the Red Cross and other volunteer war services, and in arrangements of reservations and accommodations for its members.

XII.

That none of the normal activities or the war-time activities of the Plaintiff were conducted for

the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities.

XIII.

It has been the policy of the Plaintiff to expend on services all its annual receipts, and during 1943 and 1944 [143] it was prevented from so doing only by reason of wartime restrictions. That in the 16-year period from and including 1931 to 1946 the Plaintiff has had a deficit in 8 years and a surplus in 8 other years.

XIV.

That the Plaintiff has never distributed, set aside, or credited on its books by way of dividends or from its earnings any money to any of its members as an incident of their membership in the Plaintiff association. That there has never been any intention to distribute any net income direct to the members. That the directors of Plaintiff serve without financial remuneration.

XV.

That the members of the Plaintiff association collectively defray all its expenses by the payment of identical membership fees and dues.

XVI.

That the Plaintiff is a continuing organization whose members make common cause both in a financial sense and in carrying out its stated purposes by group activity as well as by individual action.

XVII.

That Plaintiff has annual meetings of its members, meetings of its board of directors, and other meetings occasionally called by the Plaintiff and its standing committees, which meetings members are entitled to attend. Other than these meetings the Plaintiff has no social features. Membership is open to all owners of automobiles unless they are considered too old, have a bad traffic record, or are otherwise irresponsible. No social, racial or religious discrimination is made with respect to membership. [144] No memberships in Plaintiff are held by any other associations, clubs or organizations. No memberships in Plaintiff association are held by operators of trucks or commercial motor vehicles as such.

XVIII.

That Plaintiff association is now and at all times pertinent hereto was certified as a "Motor Club" by the State of California.

XIX.

That Plaintiff association is a club.

XX.

That Plaintiff association is a separate and distinct organization from the California State Automobile Association Inter-Insurance Bureau. Although Plaintiff and said Bureau jointly occupy the office quarters of Plaintiff association, said Bureau compensates Plaintiff for the space the former occupies, on a square foot basis, and Plaintiff derives no profit or earnings from its relationship with said Bureau.

From these facts the Court concludes:

CONCLUSIONS OF LAW

I.

A club is an association the expenses of which are shared among its members. Equivalence between the proportion of a member's contributions and the benefits which he enjoys is of no moment as long as there is payment by him for the repeated use of its facilities available to the members. Plaintiff is such an association.

II.

To constitute a club within the meaning of Section 101 (9) of the Internal Revenue Code it is not necessary that [145] its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity. Plaintiff meets these requirements.

III.

Plaintiff association is and was at all times here pertinent a club within the meaning of Section 101 (9) of the Internal Revenue Code.

IV.

A club operated for pleasure or recreation is one in which the members carry out or enjoy those common purposes acting either individually or collectively. Plaintiff association is such a club.

V.

Specific activities and services of Plaintiff which if performed by others might be deemed of a com-

mercial or profitable nature are, as carried on by Plaintiff, performed for purposes of pleasure and recreation of its members and not for profit.

VI.

The mere receipt of money, by an organization exempt under Section 101 (9) of the Internal Revenue Code, as a result of incidental activities, or in insignificant amounts, is not sufficient to destroy the exemption under that Section so long as the money is expended for exempt purposes. It is the destination and not the source of the income which governs the right to exemption.

VII.

The Plaintiff association was not organized or operated for the purpose of making a profit or building up a surplus [146] for the benefit of itself or its members.

VIII.

Neither the pleasure and recreation nor the non-profitable nature of Plaintiff's objectives and purposes is destroyed by its members' occasional use of its facilities and services for their individual business purposes.

IX.

The excess of receipts over expenditures of Plaintiff association resulting from the unavoidable curtailment of Plaintiff's services during any year did not constitute "net earnings" within the meaning of Section 101 (9) of the Internal Revenue Code, and did not inure to the benefit of any member of Plaintiff.

X.

Non-profitable purposes within the meaning of Section 101 (9) of the Internal Revenue Code are not changed to profitable purposes by the mere fact that in some years the receipts of Plaintiff exceeded its expenditures.

XI.

Plaintiff association was organized and operated exclusively for pleasure, recreation and other non-profitable purposes during the years 1943 and 1944.

XII.

No part of the net earnings of Plaintiff association inured to the benefit of any of its members during the years 1943 and 1944.

XIII.

Plaintiff is entitled to judgment as prayed.

DAL M. LEMMON,
Judge.

Dated March 24th, 1948.

[Endorsed]: Lodged 3/12/48. Filed March 24, 1948. [147]

In the District Court of the United States In and
For the Northern District of California,
Southern Division

No. 26,017-L

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,

Plaintiff,

vs.

JAMES G. SMYTH, Collector of Internal Reve-
nue, of the First Internal Revenue Collection
District of California,

Defendant.

JUDGMENT

This cause came on regularly to be heard before the Court, sitting without a jury, on the 25th day of June, 1947. Plaintiff was present in Court and represented by its counsel, Arthur H. Deibert and George E. Sandford, and the Defendant was present in Court and represented by his counsel, William E. Licking, Assistant United States Attorney for the Northern District of California. Thereupon oral and documentary evidence was submitted by and on behalf of the parties to the action and at the conclusion of all the evidence both of the parties rested and the cause was submitted to the Court for its consideration and decision, and thereafter the Court, having fully considered the same and being fully advised in the premises, made and ordered entered and filed its Findings of Fact and

Conclusions of Law, which are here referred to.

Wherefore, by reason of the law and the evidence and the Findings of Fact and Conclusions of Law of the Court and the premises aforesaid, It Is Ordered and Adjudged and this does order and adjudge that the Plaintiff have judgment exempting it from the payment of income tax and excess profits tax for years 1943 and 1944, and that Plaintiff have and recover of and from the Defendant named above the total amount of \$232,865.12, plus interest thereon from September 15, 1945, until paid, together with the costs of Plaintiff necessarily incurred herein and hereby taxed in the sum of \$27.00.

Done and dated at San Francisco, California, this 24th day of March, 1948.

DAL M. LEMMON,

United States District Judge.

[Endorsed]: Filed March 24, 1948.

Entered in Civil Docket 3/25/48. Vol. V—Page 380. [149]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given, that the Defendant James G. Smythe, Collector of Internal Revenue, hereby appeals to the United States Circuit Court

of Appeals for the Ninth Circuit from the final judgment made and entered herein on March 25, 1948 in favor of the above Plaintiff.

Dated May 20, 1948.

/s/ FRANK J. HENNESSY,
United States Attorney,

/s/ WILLIAM E. LICKING,
Asst. United States Attorney.
Attorneys for Defendant,
James G. Smythe.

[Endorsed]: Filed May 20, 1948.

[150]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET

Good cause appearing therefor,

It Is Hereby Ordered that the Defendant herein may have to and including August 18, 1948 within which to file the record and docket the cause in the appeal of the above case.

Dated June 29th, 1948.

LOUIS E. GOODMAN,
United States District Judge.

[Endorsed]: Filed June 29, 1948.

[151]

Undocketed

In the United States Circuit Court of Appeals
for the Ninth Circuit

Civil No. 26017-S

JAMES G. SMYTH, Collector of Internal Revenue
of the First Internal Revenue Collection
District of California, Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a Corporation, Appellee.

ORDER OF COURT

The affidavit of William E. Licking, Assistant
United States Attorney, requesting an extension
of time within which to file and docket the record
in the appeal of the above case, having been read
and filed, and good cause appearing to the Court
therefor;

It is hereby ordered that the time within which
Appellant shall file and docket the record in the
appeal of the above case shall be extended to and
including September 18, 1948.

CLIFTON MATHEWS,

Judge of the Circuit Court of Appeals for the Ninth
Circuit.

[Endorsed]: Filed Aug. 17, 1948. Paul P.
O'Brien, Clerk.

A True Copy, Attest: Aug. 17, 1948.

(Seal) PAUL P. O'BRIEN,
Clerk,

By FRANK H. SCHMIDT,
Deputy Clerk.

[Endorsed]: Filed Aug. 18, 1948. C. W. Cal-
breath Clerk. [152]

[Title of U. S. Court of Appeals and Cause.]

ORDER OF COURT

The affidavit of William E. Licking, Assistant United States Attorney, requesting extension of time within which to file and docket the record in the appeal of the above case having been read and filed, and good cause appearing to the Court therefor;

It is hereby ordered that the time within which Appellant shall file and docket the record in the appeal of the above case shall be extended to and including October 7, 1948.

CLIFTON MATHEWS,
Judge of the Circuit Court for the Ninth Circuit.

[Endorsed]: Filed Sept. 23, 1948. Paul P. O'Brien, Clerk.

[Endorsed]: Filed Sept. 24, 1948. C. W. Calbreath, Clerk. [153]

In the Southern Division of the United States
District Court for the Northern
District of California

[Title of Cause.]

DESIGNATION OF CONTENTS OF RECORD
ON APPEAL

To the Clerk of the above entitled Court and to
Messrs. George E. Sandford and A. H. Diebert,
attorneys for plaintiff:

Defendant above by its attorneys hereby designates for inclusion in the transcript of record upon appeal the following:

1. The complaint and attached exhibits;
2. The Answer;
3. All of plaintiff's exhibits in evidence;
4. All of defendant's exhibits in evidence;
5. The Reporter's Transcript;
6. The Opinion and Order of the District Court; [154]
7. The Findings of Fact and Conclusions of Law;
8. The Judgment of the Court;
9. The Notice of Appeal;
10. The Order of the District Court of June 29th extending time to file and docket Record on Appeal;
11. The Order of Circuit Court extending time to file and docket Record on Appeal;
12. The Order of the Circuit Court on September 25th extending time to file and docket Record on Appeal;

13. Statement of Points Intended to be relied upon on appeal;

14. Designation of Record.

/s/ FRANK J. HENNESSY,
United States Attorney,

/s/ WILLIAM E. LICKING,
Assistant United States
Attorney,
Attorneys for Defendant.

[Endorsed]: Filed Sept. 24, 1948. [155]

[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH THE
DEFENDANT INTENDS TO RELY
ON APPEAL

Defendant hereby designates the points on which defendant intends to rely on the appeal of said cause to the United States Court of Appeals for the Ninth Circuit, this designation to be filed with the transcript of record.

1. The District Court erred in holding that the plaintiff received no income during the years 1943 and 1944 that was subject to the federal income tax.

2. The District Court erred in holding that plaintiff was, during the years 1943 and 1944, a club organized and operated exclusively for pleasure, recreation and other nonprofitable purposes within the meaning and intent of the provisions of Section 101 (9) of the Internal Revenue Code. [156]

3. The District Court erred in holding that no

part of the plaintiff's net earnings during the years 1943 and 1944 inured to any of its members within the meaning of Section 101 (9) of the Internal Revenue Code.

4. The District Court in holding that plaintiff was exempt from the payment of federal income taxes during the taxable years of 1943 and 1944 by the provisions of Section 101 (9) of the Internal Revenue Code.

5. The District Court erred in failing to give judgment for the defendant.

6. The District Court erred in holding that plaintiff is entitled to judgment in the sum stated or any judgment.

7. The District Court erred in holding that plaintiff is entitled to judgment for its costs of suit.

/s/ FRANK J. HENNESSY,

United States Attorney,

WILLIAM E. LICKING,

Assistant United States

Attorney,

Attorneys for Defendant.

[Endorsed]: Filed Sept. 24, 1948. [157]

District Court of the United States,
Northern District of California

CLERK'S CERTIFICATE

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 157 pages, numbered from 1 to 157, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of California State Automobile Association, a Corporation, Plaintiff, vs. James G. Smyth, Collector of Internal Revenue of the First Internal Revenue Collection District of California, Defendant, No. 26017-L, as the same now remain on file and of record in my office.

I further certify that the cost of preparing the foregoing transcript of record on appeal is the sum of \$62.80 and that the said amount has been charged against the United States of America.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 30th day of September, A.D. 1948.

(Seal)

C. W. CALBREATH,
Clerk. [158]

In the Southern Division of the United States
District Court, in and for the Northern
District of California

Before: Hon. Dal M. Lemmon, Judge.

No. 26,017-S

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,

Plaintiff,

vs.

JAMES G. SMYTH, Collector of Internal Reve-
nue of the First Internal Revenue Collection
District of California,

Defendant.

REPORTER'S TRANSCRIPT

Appearances: For the Plaintiff: George E. Sand-
ford, Esq., and A. H. Deibert, Esq. For the De-
fendant: William E. Licking, Esq., Assistant
United States Attorney.[1*]

Wednesday, June 25, 1947

10:00 o'clock a.m.

The Clerk: California State Automobile Asso-
ciation vs. Smyth.

Mr. Deibert: This is an income tax case involv-
ing the California State Automobile Association,
and for the years 1943 and 1944, the corporation
being on a calendar year basis.

The point in question is whether or not the Cali-

* Page numbering appearing at foot of page of original
certified Reporter's Transcript.

ifornia State Automobile Association is entitled to exemption from income taxes, and secondly, from excess profits taxes—

The Court: Well, getting down to the pleadings, I observe that in Paragraph 1—Paragraph 5 of the complaint alleges that taxes were paid on October 14, 1945—I mean September 14, 1945, and the answer denies that and alleges it was paid October 14, 1945. I don't know how material that is.

Mr. Licking: The fact is, your Honor, the taxes were not paid on either the 14th of September or in October, as we have averred; they were originally paid on the 15th day of September, 1945, and that is the fact.

Mr. Deibert: Yes, we have a stipulation, your Honor, covering that point, making the payment date September 15, 1945.

As a matter of fact, the taxes were paid with two checks, one of which was dated September 14, and the other not until [2] September 15.

The Court: The real factual issue, then, is the character of the plaintiff corporation.

Mr. Deibert: That is correct.

Mr. Licking: That is all.

The Court: Can you enter into any stipulations to narrow this issue?

Mr. Licking: Well, we have stipulated that certain documents be put in evidence. The stipulation is here any time they offer the documents. They are really in the nature of joint exhibits, so far as that is concerned.

Mr. Deibert: Yes.

Mr. Licking: Insofar as the Government is concerned, those statements show the nature of the organization, show what it was organized for, and they contain the affidavit of an officer of the Association as to the type of business in which the Association was engaged at the time. I understand the factual situation is somewhat different at this time.

Mr. Deibert: Yes, the factual situation has somewhat changed since that period. The information Mr. Licking refers to is an affidavit of Mr. D. E. Watkins, General Manager and Secretary of the Association, which was dated October 5, 1941, so that obviously it does not cover the period of the two years in suit here. We have stipulated nearly all of the documentary evidence, and I shall introduce that [3] stipulation later, but we feel it is necessary in order to present a complete picture of the history, the activities of the Association, and particularly during 1943 and 1944, to present certain oral evidence, which we shall do as rapidly as possible, and we wish to go forward with the case and conclude it just as soon as we can, today if possible. That may depend upon the amount of cross-examination, but we want to go along just as speedily as we can.

Now, for the years 1943 and 1944, and only because they were demanded to by the Commissioner of Internal Revenue, the corporation did in 1945 file income tax and excess profits tax returns for those two years and paid on account of taxes and interest up to the date of payment for the two

years—that is, including income and excess profits taxes for each of the two years, an aggregate of \$232,865.12.

We expect to show that this association was organized in 1907 as a non-profit, non-stock corporation, under the laws of the State of California, and that until a ruling was received late in September, 1944, by the Association from the Commissioner of Internal Revenue at Washington, throughout its history the Association had been considered and had been granted exemption from the payment of any income taxes.

This exemption is based on statutes which first came into the revenue laws with the Revenue Act of 1916 and has continued down to the present time almost unchanged. It is now [4] in the Internal Revenue Code and has been in that code since 1938 in Section 101(9), and which provides exemption from income taxes to certain corporations in the following language:

“Clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inure to the benefit of any private shareholder.”

That is the whole section for your Honor's consideration, so that the issue is a very narrow one.

Throughout the history of revenue legislation, beginning with the Act of 1916, this specific exemption was contained in the Act and has been continued with a very minor exception ever since. That minor exception is this: that originally the word-

ing was "private stockholder or member," and that was later changed to private shareholder. That is an immaterial change, of course.

The plaintiff in this case, we contend and we believe we can show, has always throughout its history been operated exclusively for the pleasure and recreation of its members and for other non-profitable purposes, and none of its net earnings has ever inured to the benefit of any member, nor has there ever been any intention that they should inure to the benefit of any member.

Plaintiff association is one of the best known and one [5] of the largest automobile clubs in the United States, and it has been operated ever since 1935 under the laws of the State of California and under a Certificate of Authority issued by the Insurance Commissioner of California as a motor club, and we have included in the stipulated documents certificates issued by the Insurance Commissioner to the Association as a motor club ever since the law came into effect in 1935.

We expect to show that the Association carries on a number of activities:

That it prepares and distributes free of charge to its membership a vast number of maps and other publications and services; that it has never been engaged in any profit-making operations; that it has never financed or helped to finance its members in the purchase of automobiles; it has never given to its members the right or privilege under any circumstances of purchasing automobile accessories or other supplies at a discount; it has never sold automobile supplies or accessories at a dis-

count to its members as they do in some other automobile clubs of this country.

The stipulation to which Mr. Licking has just referred contains in documentary form the history of the present controversy which arose first by a letter addressed to the plaintiff by the Collector of Internal Revenue at San Francisco on September 10, 1941, requesting a sworn statement by one of its principal officers respecting its activities, [6] the source and disposition of its income, and any other activities which might affect its tax-exempt status, which, as I said before, had been afforded it without question up to that time ever since the Income Tax Act came into existence in 1916.

In compliance with that request, Mr. D. E. Watkins, the General Manager, on October 5, 1941, executed an affidavit, which, with the exhibits, is also in the stipulation, containing a statement regarding the activities of the Association at that time and up to that time.

That was forwarded to the Collector in response to his letter.

We think it is worthy of note that the Commissioner waited almost three years before again communicating with the plaintiff with reference to income evidence and exemption. The next communication from the Commissioner was a letter dated September 23, 1944, which for the first time denied the Association income tax exemption, and notification made that such denial was retroactive to January 1, 1943, which was almost two years prior to the date of that notification.

I was retained by the Association and went to Washington for conference with reference to this matter, as a result of which I wrote a letter to the Commissioner of Internal Revenue on June 14, 1945.

We are protesting not only the withdrawing of the [7] exemption, but also protesting what we consider to be the harsh effect of the ruling in late 1944 being made retroactive to January 1, 1943, when the Association had had no information from the Department for a period of nearly three years that such exemption would be denied.

The final letter of the Commissioner denying the exemption was dated July 27, 1945, and that letter also is within the stipulation.

We believe that the denial of the exemption to this plaintiff, in common with all other automobile clubs within the United States, was an error of law, and because of the peculiar facts concerning the operation of this Association, which will be outlined to your Honor in oral testimony, we believe that we do and always have come within the tax exempt provision of the law, which as I have already pointed out, is Section 101(9) of the Internal Revenue Code, and we believe the Commissioner made his ruling on the basis of a clear misinterpretation of certain cases which he cited in support of that ruling.

We feel very strongly that the Association is entitled to exemption for 1943 and 1944, as it had been throughout its prior history, and that there should be no tax under the circumstances. The

Association did pay the tax at the time it filed its returns and then filed claim for refund, and under the Internal Revenue Code a taxpayer has the right, [8] as your Honor knows, to file a suit for the recovery of taxes so paid if the Commissioner within six months of filing of the claim has not acted on the claim. He did not so act, so we filed this suit prior to his reduction of the claim, but that followed later.

The Court: The claim for the refund was filed when?

Mr. Deibert: Pardon me?

The Court: When was the claim for refund filed?

Mr. Deibert: Claims for refund were filed—

Mr. Licking: It was filed as alleged in the plaintiff's complaint.

Mr. Deibert: What was that?

Mr. Licking: I say it was filed as alleged in the plaintiff's complaint.

Mr. Deibert: That is alleged in the complaint, your Honor. We have—

Mr. Licking: Paragraph 3, Page 5—or Paragraph 12 on Page 5.

Mr. Deibert: Yes, on or about October 3, 1945.

The Court: You say no action was taken by the Commissioner on it and six months later this action was instituted?

Mr. Deibert: Yes, that is true, your Honor.

Mr. Licking: I will make a very brief statement. Counsel has stated the situation.

In connection with the failure of the Commis-

sioner to act [9] promptly after 1941, I take it, is explained by the fact that this action was a national action taken as to all similar clubs in 1943 and had not been taken as to any of them prior to that time. There is no difference between 1941 and 1943, as far as this club is concerned, or any other club in the United States. That followed G.C.M. 23,668, which was issued in 1943. In other words, it was a change at that time of the Department in reference to all clubs.

Mr. Deibert: My information is that the action as to different clubs was taken at different times, but I am familiar with the G.C.M. to which Mr. Licking refers, which was a general ruling by the General Counsel of the Bureau of Internal Revenue.

Mr. Licking: And which reverses prior decisions, and for the convenience of the Court, and I take it Counsel has no objection, I intend to offer it.

Mr. Deibert: None whatever.

Mr. Licking: I intend to offer it.

Mr. Deibert: As a matter of fact, it is a publication—

Mr. Licking: It is published. I merely want for the convenience of the Court to supply this copy.

Mr. Deibert: Yes.

Mr. Licking: Now, there isn't any conflict about the facts in the situation, and they all appear, as I have stated before, in documentary evidence which will be submitted to [10] the Court.

The Government's position is that this is not

an association for the pleasure or recreation of its members, or for any similar purpose; that it is flatly and frankly a service club which offers to its members services which are commercially available; that there is no restriction on the membership except the ownership of an automobile and the ability to pay the dues, and that the purpose of the club is not the pleasure and recreation of its members, or is not any similar purpose, but it is flatly and frankly a service club that offers certain services to its members which are available commercially, but it offers those services to those members at a lesser price than those services would be available commercially.

That is the whole issue in the matter, whether this is a club—first, whether it is a club or association within the meaning of the Act; second—

The Court: I do not apprehend that there is very much difference between you as to the activities and character of this club. It is a matter of construction or interpretation of whether it is a club within the meaning of this provision.

Mr. Licking: Whether it is a club within the meaning of that and whether its purposes are within the meaning. There are two questions. It seems probably somewhat technical to [11] argue whether it is a club or association—

The Court: I think most of us can almost take judicial notice of the activities of the club that are so well known. I thought that you could agree on what the activities are.

Mr. Licking: My own position is that all the activities of the club are reflected properly in the

documentary evidence which we have stipulated be introduced in the case, in the evidence that Mr. Deibert mentioned here as to these things the club does not do, I think that is entirely irrelevant to this particular case, what the club does not do. It is a matter of what the club does do. That is the only issue in the case, whether it is, within the meaning of 101 of the subsection quoted, a club or association conducted for the pleasure and recreation of the members or for other similar non-profitable purposes. That is the whole question.

Up to 1943 the Commissioner apparently considered that it was such an organization. He asked for certain information, which was given him in 1941 by the company as to its activities, and in 1943 the assessments here complained were based on that information furnished by the corporation.

The Court: That information that was given, are you going to amplify that?

Mr. Licking: As far as the Government is concerned, the Government's case is in these documents.

Now, I have told Mr. Deibert it seems to me that some of [12] the evidence he proposes to introduce might clarify the situation for the Court, but certainly this evidence as to what activities the Association did not engage in I intend, of course, to object to, and I think the Court will sustain those objections, as to what activities they did not engage in.

Now, as to the activities they do engage in, it seems to me the only material thing is whether

or not there was any change in the activities of the Association for the years for which the refund is requested.

The Court: Can you stipulate to that? Is there any dispute on that?

Mr. Licking: There are certain matters that Mr. Deibert felt in that matter—and on the relevancy of that evidence I agree with him—what change there was between the situation as set out in their own statement in 1941 and the subsequent years.

The Court: What changes were there?

Mr. Deibert: Well, there are very specific changes, your Honor, but aside from that, this affidavit submitted by Mr. Watkins in October, 1941, was very brief; it didn't go into many of the details that we feel should be brought out in a case of this kind because they have a very definite and fundamental bearing upon the character of the club itself, and we do not agree that we could possibly rest our case [13] alone on the affidavit of Mr. Watkins, which was only eight or nine pages and does not contain much of the history which we intend to bring out to show the original purpose of the Association, what it did in early years. We should be very happy to stipulate if we felt that we could properly present the case on such a stipulation, but we feel we absolutely cannot.

The Court: Well, proceed then. Call your first witness.

Mr. Deibert: I wish to first introduce in evidence this stipulation together with the accompany-

ing documents and ask that it be appropriately marked.

The Court: It will be received if there is no objection.

Mr. Licking: There is none, your Honor.

The Court: And the documents are what, briefly?

Mr. Deibert: The documents contain, briefly, the original articles of incorporation, the amended articles of incorporation—

Mr. Licking: May those—I don't believe they have any distinctive marks, as they are—the are merely given a number.

The Clerk: 1-A, 1-B?

Mr. Deibert: Very well. And the letters that passed back and forth between the Association and the Collector of Internal Revenue as outlined in my opening statement; copies of the income tax returns for 1943 and 1944; copies of [14] certificates issued each year by the Commissioner of Insurance of the State of California; and then the final paragraph is a stipulation as to the correct date upon which the taxes were paid, September 15, 1945.

Mr. Licking: For the record may we formally identify these different documents. 1-A will be the articles of incorporation of the California State Automobile Association.

Mr. Deibert: Yes.

The Court: I think the Clerk has already marked them.

The Clerk: The stipulation itself is 1; 1-A is the articles of incorporation.

Mr. Licking: 1-B would be the certified copy of the resolution amending the articles of incorporation.

The Clerk: 1-C would be the letter from the Treasury Department to the State Automobile Association dated September 10, 1941.

Mr. Licking: And 1-D is the affidavit of D. E. Watkins, the Secretary of the California State Automobile Association, regarding the activities of the Association.

The Clerk: 1-D, yes. And 1-E are the compilations—

Mr. Deibert: No, the compilations, a statement of income and expenses, were attached to that affidavit as exhibits.

Mr. Licking: They are a part of the affidavit. They should be clipped together with this.

Mr. Deibert: And this (indicating). [15]

Mr. Licking: All together with the financial statements for the previous years.

Mr. Deibert: That is right.

The Clerk: That is 1-D?

Mr. Licking: 1-D, the affidavit of Watkins with the attached documents.

The Clerk: And the letter from the Treasury Department—

Mr. Licking: 1-E, dated September 23, 1944, from the Office of the Commissioner to the State Automobile Association.

The Clerk: And 1-F will be the—

Mr. Licking: Copy of the letter from Mr. Deibert dated June 14, 1945, addressed to the Commissioner of Internal Revenue.

The Clerk: That is correct. 1-G—

Mr. Licking: 1-G would be a letter dated July 27—

The Clerk: Pardon me, there is a balance sheet here.

Mr. Licking: That belongs to that (indicating).

Mr. Deibert: That belongs to my letter.

Mr. Licking: That is part of 1-F.

The Clerk: 1-G will be the letter—

Mr. Licking: Letter from the Office of the Commissioner dated July 27, 1945.

The Clerk: That is correct.

Mr. Licking: 1-H is a copy of the Income and Declared Value Excess Profits Return of the Association for the year [16] 1943. And 1-I is a copy of the return for the year 1944.

1-J is four certificates from the Department of Insurance in the State of California authorizing the California State Automobile Association to sell or contract for rendering motor club service during the years 1942, 1943, 1944 and 1945.

Mr. Deibert: No, 1947.

Mr. Licking: Is there a gap?

Mr. Deibert: Yes; we didn't put the others in there, because we just wanted to show why this last one was still in existence.

Mr. Licking: Well, the same certificates are in effect.

Mr. Deibert: That is right.

Mr. Licking: There was no change.

Mr. Deibert: No change.

The Clerk: Just one exhibit, those four certificates?

Mr. Deibert: That is right.

(The documents above referred to were thereupon received in evidence and marked Plaintiff's Exhibits 1, 1-A, 1-B, 1-C, 1-D, 1-E, 1-F, 1-G, 1-H, 1-I and 1-J, respectively.)

Mr. Licking: And then there is the stipulation which we mentioned to the Court as to the date of payment, that these taxes were actually paid on September 15, 1945.

Mr. Deibert: Now, your Honor, we have substituted for the originals—I hold the originals in my hands— [17] photostatic copies, if that is agreeable to your Honor, I think it is to Mr. Licking, to substitute photostatic copies instead of the originals.

Mr. Licking: I haven't any objection to that.

Mr. Deibert: I will furnish Mr. Licking with copies.

Mr. Licking: I have certified copies of the income tax returns here. I haven't any objection. You have, of course, the original.

The Court: Very well.

Mr. Deibert: My first witness is Irving H. Kahn.

Mr. Licking suggests the introduction of the claims for refund. We have no objection to that.

Mr. Licking: I think it will give the Court a clearer view of the situation.

Mr. Deibert: They are not denied in the answer, and we readily agree they go into evidence.

Mr. Licking: As stated, of course, this is—the suit is for recovery of income tax and excess profits

tax. I would like to offer in evidence the claims for refund for the income tax assessments for 1943; offer a certified copy.

(The document in question was thereupon received in evidence and marked Defendant's Exhibit A.)

Mr. Licking: And for excess profits tax for the same year 1943. They may be marked together.

The Court: Very well. [18]

Mr. Licking: As one exhibit. And the same claims for refund for the year 1944,—that is, for income tax and excess profits tax.

I believe that that gives the Court the entire picture, so far as the claims of the Government, the incident of the tax and the statement—I don't think there is anything out of the picture now; everything is there.

(The copies of Claims for Refund of Income Tax and Excess Profits Tax for the year 1944 were received in evidence and marked Defendant's Exhibit B.)

Mr. Deibert: Yes. Those are Exhibits A and B, are they?

The Clerk: Yes.

Mr. Deibert: Mr. Kahn.

Mr. Licking: The other exhibits, I take it, were joint exhibits?

Mr. Deibert: That is right.

IRVING H. KAHN,

called as a witness on behalf of the plaintiff; and being first duly sworn, testified as follows:

Direct Examination

Mr. Deibert: Q. Where do you reside, Mr. Kahn?

A. In San Francisco, at 3364 Washington Street.

Q. In what business are you now engaged?

A. I am an officer and director of several corporations, but [19] primarily engaged as business counsellor.

Q. What is your business address?

A. 300 Montgomery Street in San Francisco.

Q. Are you a member of the California State Automobile Association? A. I am.

Q. Have you ever held any office in that association?

A. I have been on the Board of Directors for something over twenty-five years and during that period served several terms as Treasurer, three terms as Third Vice-President, two terms as Second Vice-President, and in 1943 and 1944 served as President.

Mr. Licking: If you are attempting to qualify the witness as familiar with the affairs of the Association I am willing to stipulate he is.

Mr. Deibert: Yes, very well.

Q. Do you now hold any office in the Association?

A. I am a director of the Association and Chairman of the Executive Committee.

(Testimony of Irving H. Kahn.)

Q. What were your duties as President?

A. Besides the—

Mr. Licking: What is the purpose of this question, to qualify the witness?

Mr. Deibert: Well, to have him explain what he did during his term of office, which encompassed the period of two years [20] involved in this suit.

A. Besides the great majority of proceedings at meetings of the Board, I was in constant touch with the executive staff in the general working out of policies, consultations on matters of operation during the war years, most of which time I was involved in making radical changes from our normal operations to meet war time conditions, making recommendations to the Board of Directors, most of which recommendations were acted on favorably.

Q. And you have been a member of the Association for how long?

A. For 37 years. I joined in the spring of 1911. I am now in my 37th year.

Q. How long have you been an operator of a motor car?

A. I had my first car in the late summer of 1910.

Q. What was your reason for joining the Association?

Mr. Licking: That is objected to as immaterial.

The Court: Sustained.

Mr. Licking: —what his reason was for joining the Association.

The Court: Sustained.

Mr. Licking: That has nothing to do with the issue in this case.

(Testimony of Irving H. Kahn.)

The Court: Sustained.

Mr. Deibert: Pardon me?

The Court: Sustained. [21]

Mr. Deibert: It seems to me, your Honor, the reason for this witness joining the Association is material, because he will testify, I think, as to what conditions were at that time, what induced him to join the Association, what type of organization it was, and what benefits he expected.

The Court: I do not see what his reasons for joining would have to do with it, what bearing upon the issue here. I am only interested in the activities of the Association and its character. His reasons for joining are immaterial. Sustained.

Mr. Deibert: May I have an exception, your Honor?

The Court: You may.

Mr. Deibert: Q. Did you receive any salary or other compensation for services as President?

Mr. Licking: Same objection.

The Court: Same ruling, immaterial.

Mr. Deibert: Are you familiar with the various activities of the plaintiff during the years 1943 and 1944, as well as from 1911 when you joined, and since 1944? A. I am, sir.

Q. Did you participate in planning or establishing such activities in 1943 and 1944?

A. Yes, sir.

Q. What did you do in that connection?

Mr. Licking: It is immaterial, if the Court please what [22] was planned to be done. What is material is what was done.

(Testimony of Irving H. Kahn.)

The Court: I think so. Sustained.

Mr. Deibert: May I have an exception, your Honor?

The Court: Very well.

Mr. Deibert: Q. What were the activities of the plaintiff during 1943 and 1944?

Mr. Licking: Calls for a self-serving declaration, if the Court please.

The Court: Overruled.

The Witness: A. The Association continued in 1943 and 1944 rendering the general type of service which it had rendered for many years past to its members in order to facilitate the use of their pleasure cars and to make possible adequate use of them. The activities of the Association had been before, and were continued during that period, in the matter of legislation affecting highways, construction of highways, the laws and regulations which control speed limits and the enforcement of the law as it related to speed limits. It provided out of its own funds a substantial—

Mr. Licking: If the Court please, while the objection does not come properly, I admit, this is not responsive and is a self-serving declaration on the part of an officer of the corporation. He answered the question. He said the activities were the same as they had been before and were the activities for which the organization was formed. The [23] question is answered, and the rest of this is just—

Mr. Deibert: But he did not outline what those activities were, Mr. Licking.

Mr. Licking: They are outlined in your Exhibit

(Testimony of Irving H. Kahn.)

1. I take it you are not engaged in any extra-curricular activities; that is, the activities are confined to the activities set out in the articles of incorporation, and the purposes.

Mr. Deibert: That is true, of course. The Association did not go beyond the scope of the chartered powers; but those are very general and they are not outlined in detail in the charter.

Mr. Licking: If the Court please, I would like to call the Court's attention to Exhibit 1.

The Court: That is the one that is attached to the—the stipulation?

The Clerk: Articles of Incorporation.

Mr. Licking: Yes, Exhibit 1 is attached to the stipulation, Articles of Incorporation.

Paragraph 2 states plainly enough what the purposes for which the corporation was formed are, and I think the corporation did not engage in any other activities than those set out there.

Mr. Deibert: It does not state them in detail, your Honor, and we think the Court should be informed in detail as to what the corporation did.

The Court: Overruled.

The Witness: May I have the last few words of my answer so I can get the connection?

Mr. Licking: I would like the question read.

(Record read.)

The Witness: A. (Continuing): It provided out of its own funds a contribution toward the signing of highways, it furnished its members with maps and travel information as to all conditions;

(Testimony of Irving H. Kahn.)

it publicized to its members the many regulations which had developed as a result of the war and then devoted the greater part of its energies to cooperating with its members in the many problems of gas rationing, securing of parts in the way of repairs, to put all of its facilities at the disposal of the Federal Government and became an official agency of the Federal Government in the signing of highways in relation to dimouts and blackout areas; in preparing special maps for its members who had to make necessary trips during the war. It continued as far as possible to inspect roadside lodgings, to make reservations for its members and to keep them informed of road conditions.

Due to war conditions it restricted many of its operations by limiting their operations to those things—

Mr. Licking: I don't like, if the Court please, to interrupt; however, the last response of the witness there certainly is not answering any question and certainly is [25] argumentative. The question was, what activities he was engaged in.

The Court: That is what we are interested in, what activities were engaged in. The reasons for engaging in them are not material.

Mr. Licking: That is what I had in mind, your Honor.

The Court: If you will confine your answer to the activities.

The Witness: A. All right. While normally our activities were limited to serving our members,

(Testimony of Irving H. Kahn.)

we undertook to serve all members of the armed forces who came into our territory in the matter of providing highway information, reservation service, and other services, and furnished the same services without cost to any person representing that they were coming into our territory seeking or having secured Government employment.

Mr. Licking: That is a nice, patriotic gesture, if the Court please, but it seems to me hardly relevant.

The Court: Do you move to strike it out?

Mr. Licking: Yes.

The Court: Denied.

The Witness: A. We undertook without charge to train the volunteer drivers of the American Red Cross and the American Women's Volunteer Service. And beyond these things we voluntarily did, we actually had the Army come in and [26] commandeer one entire floor of our building, and we housed them without knowing whether we would or would not receive compensation.

Mr. Licking: If the Court please, it seems to me this is not a statement of activities at all. This is a sort of rambling narrative.

The Court: I think it has a bearing on the activities. Proceed.

The Witness: A. In the course of our normal activities we undertook to protect the interest of our members in the matter of when they are involved in accidents, of adjusting for them the damages with a third party. If they are unfortunate

(Testimony of Irving H. Kahn.)

enough to be involved in an arrest, we continued to appear in court to represent them.

Going back for just one moment to the matter of our activities during the war, and while it is not activities, if it is not out of order I would like to go back to say—

Mr. Licking: If the Court please, I understood that was the only question that the witness was supposed to be answering, that is, the activities of the Association during the period here concerned.

The Court: The witness' conclusion as to whether it was or was not an activity may or may not be correct—but you understood the question—

The Witness: A. I understood the question.

The Court: —to define the activities of the [27] Association?

The Witness: A. I was trying to indicate, your Honor, that the type of activities in many cases were restricted because of war conditions and that we diverted equipment and man power from the recreational signing of our highways to the signing of highways for military purposes.

Mr. Licking: It seems to me that is entirely non-responsive and self-serving, and should be stricken.

The Court: Well, the motion is denied. Proceed.

The Witness: A. We provided emergency road service for our members if they met with disaster on the highways or had mechanical trouble that they could be taken in off of the highway to the

(Testimony of Irving H. Kahn.)

nearest place of garaging and servicing; we maintained a register of automobile repair shops which we had investigated and where we were able to certify to our members that we believed that the charges there would be reasonable, and if the charges were not, we would undertake to adjust any complaints which arose.

We continued to investigate and recommend places of lodging. We undertook to secure reservations for our members and members of the armed forces who were traveling in the area, reservations at those places which were difficult to obtain.

We continued to provide a service for the renewal of membership licenses, and continued our general activities [28] that we had rendered over the years.

Mr. Deibert: Q. To whom were these services rendered?

A. Normally, sir, to the members of our Association, and members of affiliated clubs of the American Automobile Association. They were extended, as I stated previously, to members of the armed forces and the volunteer workers of the American Red Cross and volunteers of the AWVC, American Women's Volunteer Corps.

Q. What was the purpose of rendering these various services?

Mr. Licking: Objected to as immaterial what the purpose was.

The Court: Sustained.

Mr. Deibert: May I have an exception, your Honor?

(Testimony of Irving H. Kahn.)

Q. Were the activities of the Association and services to members normal in 1943 and 1944?

Mr. Licking: Objected to on the ground it has been asked and answered. He stated the services were not normal and explained how they were not normal.

The Court: Yes. Is there any further explanation you want to make as to the difference between the activities before and during that period? Have you fully explained it?

The Witness: A. I have explained the activities, yes, sir.

Mr. Deibert: Q. The change in activities?

A. Yes, sir. [29]

Mr. Deibert: That is all.

Cross Examination

Mr. Licking: Q. Your answer in brief to the questions propounded by Mr. Deibert is that during the period covered here, in 1943 and 1944, you continued so far as war conditions permitted, in the same activities you had engaged in before? That is your answer, isn't it?

A. The same activities in relation to services rendered our members.

Q. Yes. Now, when you described the activities of the Association with reference to the services rendered to your members, did you intend that to be comprehensive, or did you just mention certain services?

A. I mentioned the main services, but I did not attempt to enumerate all of them.

(Testimony of Irving H. Kahn.)

Q. You did not attempt to enumerate all of them? A. No.

Q. That is, there were other things during that period? You furnished some help or assistance in the matter of insurance during that period, did you not?

A. Not as part of the California Automobile Association.

Q. Not as part—well, how did you do it? You say not as part of the California State Automobile Association. How did you furnish that service?

A. Well, the California State Automobile Association did not [30] furnish any insurance services.

Q. You say not as part—I asked you if the Association furnished any insurance service to its members, and you said, not as such.

A. The answer should have been “No”, then, sir.

Q. It should have been “No”. What did you mean when you said “not as such”?

A. I assume, sir, you mean the Inter-Insurance Bureau which is composed of certain members of the California State Automobile Association.

Q. May I ask just one other thing in connection with that: Is it not a fact that that is composed solely of members of your Association?

A. It is composed solely of members—

Q. Solely of members of your Association?

A. Not all members.

Q. Any member of your Association that wishes

(Testimony of Irving H. Kahn.)

to avail themselves of the services of the Inter-Insurance Bureau may do so, and nobody that is not a member of your Association may do so, is that correct?

A. As to your first statement, I think there must be a qualification: If a member has a record of hazardous driving or bad insurance record, I am sure he cannot avail himself of that service. As to the second part: No one can avail himself of the services of the Inter-Insurance Bureau unless he [31] is a member of the California State Automobile Association.

Q. To that extent, then, the insurance service, while not furnished by the Association, is incident to membership in the Association, it is a privilege which is restricted to members of the Association?

A. It is not even extended to all members of the Association.

Q. Pardon me, but so far as it exists, it is a privilege of membership in your Association?

A. I wouldn't be able to answer that.

The Court: It is a privilege extended only to members?

The Witness: A. That is correct, it is a privilege extended only to members of our Association.

Mr. Licking: Q. Well, now, you furnish legal advice too, do you not?

A. I don't believe so.

Q. You don't? What were you talking about, traffic violations in court, advice as to the effect of statutes? I understood you to answer you did that.

(Testimony of Irving H. Kahn.)

A. I think I stated the service, sir, was one that if a member of our organization was involved in an accident either with a member or a non-member, we would attempt to adjust the financial responsibility between the two of them, and further, that where a member of ours is involved in an arrest under certain conditions we make an appearance in court to plead for him. [32]

Q. You don't consider those little items to be legal? Aren't those legal services? I asked you if you extended legal services to members and you said no. You now say you do furnish them. Is this lay advice or professional advice? Do you have attorneys for that purpose to advise them?

A. Again, sir, the matter of advice—I am again repeating, if a member is arrested for an infraction—

Mr. Licking: Oh, I will withdraw the question. I don't wish to argue the question. You used the word "advice". You say if the members are arrested or if the members are involved in an accident, that someone comes to adjust the situation. All I am interested in is finding out who this somebody is. Is it an attorney?

A. We have a staff of employees who are attorneys for that purpose, admitted to the Bar of California.

Q. I see. And they give this type of service that you have just described to your members?

A. Yes, sir. [33]

Q. And with reference to your servicing cars

(Testimony of Irving H. Kahn.)

on the road, and your relation to garages, you said something in that connection.

A. We contract with garages to render emergency road services to our members. The member receives that service, identifies himself and signs a tag showing the receipt of the services.

Q. You contract the garages?

A. We contract with garages. When that service has been rendered, at stated periods the garage bills us for the services rendered to our members, and we make the payment to the garage.

Q. And you bill your member?

A. We do not.

Mr. Licking: In other words, if the Court please, not that it would make any difference in the situation, I am wondering if by chance the court may be a member of the association.

The Court: I am not.

Mr. Licking: I know my wife is, but I don't think that would disqualify either one of us.

Mr. Deibert: I think not.

Mr. Licking: Q. That is in connection with the legal situation, in connection with service. Now, in the matter of this road service: As a practical matter—

Mr. Licking: I had hoped that the court was a member of the association. [34]

The Court: How is that?

Mr. Licking: I had hoped that the court was a member of the association so I wouldn't have to go through the activities here and the court could practically take judicial notice of them.

(Testimony of Irving H. Kahn.)

Q. If one of your members broke down on the road—

The Court: Many, many years ago I happened to be one of those attorneys to whom you made reference.

Mr. Licking: Q. Well, your member does not pay the attorneys? A. He does not.

Q. You pay them? A. Yes, sir.

Q. Your member does not pay the garage for the towing service; you pay them?

A. Yes, sir, we pay them.

Q. Well, now, is there any other service, that is, describing it in practical terms, that you can think of that you have not told the court about, other than legal advice, both in civil and criminal cases?

A. I am sorry, sir, I don't want to quibble over the word "legal advice".

Q. Now, wait a minute, I will withdraw that word, I don't want to get into that argument again, but you do hire attorneys?

A. We do hire attorneys. [35]

Q. And those attorneys do—

A. Adjust controversies involved in accidents and attempt to settle without going into court the action or damage claim, if I remember, claims that he was in the right and the other man was in the wrong.

Q. And that is something which you do not consider to be legal advice?

A. I wouldn't use the word "advice".

(Testimony of Irving H. Kahn.)

Q. You wouldn't use the word "advice". What would you use if you wouldn't use the word "advice"?

A. I would call it an adjustment service. I have never understood—

Q. A legal adjustment, right?

A. I wouldn't say—

Q. Well, these attorneys, again, isn't whatever they do legal? A. I hope it is, sir.

Q. Well, all right. Is not what they do service?

A. It is a service.

Q. Then it is legal service, rather than legal advice?

A. I answered the word I hoped their actions were legal actions. It is my understanding that if anyone had an accident that we—

Q. I didn't ask for your understanding. Are we agreed that what you did furnish is legal services? Do we agree on that? A. No.

Q. That is the word you used. [36]

The Court: I think you are wasting a lot of time, Mr. Licking. You have brought out from the witness what services were rendered. I think you will have to leave it up to me to determine whether they are legal services, if that is necessary.

Mr. Licking: That is true, but my idea was it was advice, and the witness does not like that word, and I was just trying to find some word he would use himself to describe it, and he contends the description of the facts is sufficient, and I guess legally he is right.

Q. Now, how about the criminal situation, or I

(Testimony of Irving H. Kahn.)

mean the traffic violations? What does your legal staff do for your members in that connection?

A. Someone representing the Association will appear in a remote place and enter a plea for someone who has been arrested, let's say, for going through a red light. The judge will assess the fine, the Association will pay the fine, and will bill the member for the money advanced to his account.

Q. Now, are there any more services than these you have mentioned?

A. To my knowledge, sir, no.

Q. If a member is in an accident or in a traffic violation your attorneys serve him as you have described, as you say?

A. In the event of arrest I understand it is limited to pleading guilty for the offender and accepting the fine.

Q. Do you advance the fine? [37]

A. They advance the fine and I reimburse it.

Q. You advance the fine to the member?

A. Pardon me?

Q. You advance the fine to the member?

A. They pay the fine into court and charge the member and collect from the member.

Q. What is the recreational and social aspects of your services?

A. Our membership is primarily made up of owners of pleasure cars. The services we render make it easier to make use of the highways, it makes it possible for them to go out on their days off and seek the recreation they are looking for.

(Testimony of Irving H. Kahn.)

We advise them as to road conditions, as to weather conditions, we advise them as to the best places to stay in, we furnish them with maps showing the best way to get there; while if they are in difficulty through a breakdown, to keep them from being stalled on the road for hours, as they used to be, we provide certain garages with which we have contracts that serve them; they will pull them off the road to the garage, and also these garages facilitate their getting parts for repairs. If they are involved in an accident we will try to minimize the disaster of the accident by trying to adjust it for them.

We certainly undertake a program of publicity on safe driving. We spend a great deal of money on the maintenance of safety controls to cut down the incident of accident, and it would seem to me that those do contribute to the pleasure, the [38] relaxation and the pleasure of the member.

Q. And social activities: I asked you two things; that, I suppose, is your explanation of the recreational activities of the members of your Association, that is the recreational activity of the Association. What about the social purposes?

A. We have no social activities.

Q. No social. What do all these what are termed services to your club members cost?

A. In normal years they cost—

Q. May I restrict the question to what did those cost during the years 1943 and 1944, the period under consideration here?

A. I would have to refer, sir, to the treasurer's

(Testimony of Irving H. Kahn.)

report to give you the figures involved, as to the expenditures by classification.

Q. My question isn't that. I asked what it cost the members.

A. I beg your pardon, sir. Our membership dues are \$12 per year, were in 1943 and 1944, and at that time a new member joining the association paid \$3 initiation, which applied only to the first year. Thereafter his dues were \$12 a year.

Q. This \$18 a year would take care of all the services rendered by the club to the members which you have described? A. How much, sir?

Q. 18—\$15 a year at that time for the first year, \$3 initiation fee, and \$12 dues.

A. That would depend on the break of conditions of the particular [39] year.

Q. Well, during these particular years was that the cost?

A. During these particular years we did not expend as much as \$15 per member per year.

Q. I didn't ask you what you expended, I just asked you what all these services cost the members during those years.

A. His dues, which were either 12 or \$15.

Q. Yes. In the first year it was initiation and membership. Is your membership in any way restricted?

A. Our membership is open on invitation and solicitation.

Q. Your membership is open on invitation and solicitation, what do you mean by that? I don't

(Testimony of Irving H. Kahn.)

understand that answer, your membership is open on solicitation.

A. We solicit our members, sir. We don't set up booths and ask every Tom, Dick and Harry to join.

Q. Well, I asked you if you have any membership requirements. In order for anyone to join you have to ask them to join?

A. I think, sir, we invite all people to join.

Q. Well, I mean as a matter of race, color, or creed.

A. No.

Q. Are there any membership requirements other than the fact that a person have a car, and no criminal record?

A. Well, I think the word "criminal record" might involve a record of reckless driving.

Q. That is what I had in mind. [40]

A. I believe—

Q. Would one matter of reckless driving prevent a fellow from joining your association?

A. It might, depending on the circumstances.

Q. What circumstances, that is, the nature—

A. I mean the nature of the thing, the nature of the offense, drunk driving.

Q. In other words, the mere fact a person has a traffic record would not prevent him from joining?

A. That would not prevent him from joining.

Q. In other words, he has to have something that is tantamount to a criminal record, you have to be convinced that he is criminally negligent?

(Testimony of Irving H. Kahn.)

A. I would say that the average owner of an automobile who has a car that is not too old, a man who seems to be of some responsibility in his community would be accepted to membership in the association, and probably would be solicited.

Q. Do you make any investigation of the person's standing?

A. Well, most of our members, I believe, come through references of other members.

Q. I asked you do you make—you spoke of a person of standing in his community. I am just asking you if you make any inquiry to find that out.

A. Well, I understand that a general application is made out, and the acceptance of the individual member depends on [41] the survey or review of that application.

Q. You understand that?

A. It is my recollection that that is the way it was done.

Q. That is the way it was done?

A. During 1943 and 1944.

Q. Isn't it a fact that anybody that has an automobile and has not a criminal record may join your association, irrespective of his social standing, his color, race, or creed? As a matter of fact, you haven't any social requirements?

A. We haven't any social requirements, but when we have an influx of strangers to a community we are very careful in including them.

Q. Did you exclude the Okies?

(Testimony of Irving H. Kahn.)

A. We did.

Q. You never made any color restrictions?

A. We have never adopted a policy.

Q. Pardon?

A. We have never adopted a policy.

Q. But you did exclude the Okies? Are you sure of that?

A. I am sure we had people from the South, and they may be both black and white, who came here during the immigration during the war and we refused to admit them to membership.

Q. Did you refuse to take them for any other reason than the fact that they did not have cars that were in proper operating order? It wasn't anything social? [42]

A. No, sir.

Q. It was due to the operative condition of their cars rather than the fact that they came from Oklahoma, or Arkansas?

A. I don't know of any person that was excluded because of the fact that—

Q. Well, let's put it this way: If a person has a car that is in proper operating condition and does not have any criminal record, that is all the requirements for membership?

A. Generally, yes.

Mr. Licking: May I have your Honor's indulgence?

The Court: Very well.

Mr. Licking: If your Honor please, this is Mr. Norton, agent of the Internal Revenue, who made the investigation.

(Testimony of Irving H. Kahn.)

Q. There may be other privileges of membership other than you have described to the court?

A. I think I have—

Q. But so far as you recall you have discussed them all?

A. We have discussed the major ones.

Q. We have discussed the major privileges of membership and we are agreed it is not a social organization, and you have described the recreational aspects to the court?

A. Yes, sir.

Q. What you consider were the recreational aspects. Now, there are certain assets, I take it, buildings; those are all reflected in your statements that are in evidence before [43] the court?

A. Yes, sir.

Q. Has a member, if you know, any right upon dissolution of your organization, should such a thing happen, has a member any right to participate in the distribution on dissolution?

A. I believe that he has.

Q. There is no provision in your bylaws for that participation on dissolution on the part of a member, is there?

A. I don't recall.

Q. When you say you believe that to be the fact that is the general understanding among your membership and the officers of the association?

A. I think it has been the understanding of the officers.

Q. That has been the understanding of the officers and you have been there for some 35 years as one of the officers?

A. Yes, sir.

(Testimony of Irving H. Kahn.)

Q. You feel that a member has that right in the event such a thing should happen?

A. Yes; he would get a brick out of the building.

Q. Yes, or a dollar out of the bank?

A. Maybe a dollar out of the bank.

Mr. Deibert: Your Honor, it seems to me that is a mere statement of a legal conclusion, and that the rights of the members are to be determined by the articles of incorporation.

The Court: No question about that. [44]

Mr. Licking: The reason for asking the question, your Honor, was that the by-laws were silent in that respect, and I was asking what the understanding was.

The Court: You are asking for the witness' legal conclusion.

Mr. Licking: I asked what the understanding of the officers were in that connection.

The Court: I think the understanding of the officers would be immaterial.

Mr. Licking: I think I have no further questions.

Mr. Deibert: I move that the testimony as to the understanding of the officers and the witness' own understanding be stricken.

The Court: As to this legal conclusion to which you have made reference?

Mr. Deibert: Yes.

The Court: Your motion is granted. Is that all from this witness?

Mr. Licking: I have no further questions.

(Testimony of Irving H. Kahn.)

Redirect Examination

Mr. Deibert: Q. Mr. Kahn, with reference to the services rendered to members if they are charged with any traffic violation, do the attorneys representing the association ever represent the member at a trial of such a case?

A. Not to my knowledge, sir.

Q. Also with reference to the Interinsurance Bureau, is that a [45] separate organization from the association, itself? A. It is, sir.

Mr. Deibert: That is all, your Honor.

Recross Examination

Mr. Licking: Q. Just a moment. With reference to the Interinsurance Bureau, can you state whether or not the member availing himself of that service secures insurance which ultimately costs him less than it would cost him if taken on the open market through a regular agency?

A. The Interinsurance Bureau endeavors to serve its members at cost, and if at the end of the year their income exceeds all expenses, payment of losses, and setting up of the reserves required by the State, in those years the member will receive a refund.

The Court: That is hardly responsive to the question. As I understood the question, it is whether or not the insurance costs the members less than they would have to pay elsewhere.

(Testimony of Irving H. Kahn.)

A. In the years in which the member receives a refund it will cost him less than his insurance would cost him in the so-called board or conference companies. It might not cost him less than it would cost him in non-board companies, or other cooperative insurance activities.

Mr. Licking: Q. In other words, this is a participating insurance, I take it? [46]

A. That is the practical effect.

Mr. Licking: I think I have no further questions.

Further Redirect Examination

Mr. Deibert: Q. Mr. Kahn, there are other interinsurance organizations from which your members, as well as other individuals, may obtain insurance under similar circumstances, are there not?

Mr. Licking: To which I object on the ground it is immaterial.

The Court: Sustained.

Mr. Deibert: That is all.

The Court: Gentlemen, it is about the time for recess. We can resume at 1:45, if that is convenient.

Mr. Deibert: That is agreeable, your Honor.

Mr. Licking: I will be glad to resume at 1:45.

(A recess was thereupon taken until 1:45 o'clock p.m.) [47]

Afternoon Session, June 25, 1947, 1:45 p.m.

Mr. Deibert: Q. Mr. Watkins, please take the stand.

DAVID E. WATKINS,

called as a witness on behalf of plaintiff; sworn

Direct Examination

Mr. Deibert: Q. Where do you reside, Mr. Watkins? A. My home address?

Q. Yes. A. Marin County.

Q. By whom are you now employed?

A. How is that?

Q. By whom are you now employed?

A. California State Automobile Association.

Q. Would you hear me a little better if I came closer? In what capacity?

A. Secretary and general manager.

Q. What is your business address?

A. 150 Van Ness Avenue, San Francisco.

Q. How long have you been employed by the California State Automobile Association?

A. Since 1913.

Q. How long have you been secretary and general manager? A. Since 1913. [48]

Q. Are you the D. E. Watkins who verified the complaint in the suit in which you are now testifying? A. I am.

Q. What are your duties as general manager and secretary?

A. Well, to supervise all the activities of the organization, particularly to ascertain the desires of the membership and formulate policies that are submitted to the board.

Q. Is the association incorporated?

A. Yes.

(Testimony of David E. Watkins.)

Q. On what date was it incorporated?

Mr. Licking: If the Court please, that is in the articles of incorporation.

The Court: That is in the exhibits.

Mr. Deibert: Pardon me?

The Court: That is in your exhibits.

Mr. Deibert: Yes, that is true, your Honor.

Q. Did you ever issue any stock to members?

A. Any which?

Q. Stock. A. No.

Q. Has your association ever qualified under the laws of California as a motor club? We have already introduced into evidence the certificate of—

Mr. Licking: Mr. Deibert, to which statute of California do you refer? I want it for the convenience of the court. [49]

Mr. Deibert: Yes, it is Chapter 2—no, Part 5, Motor Clubs, of the Insurance Code of the State of California, your Honor, beginning with Section 12140 of the Insurance Code.

Q. You have had these annual certificates issued to your association by the insurance commissioner every year, have you, since 1935, down to and including the present? A. That is right.

Q. Have any such certificates ever been rescinded? A. No.

Q. Is such a certificate still in effect?

A. Yes.

Q. Are you familiar with Part 5, entitled, "Motor Clubs", of the Insurance Code of California, defining a motor club and Motor Club Services in Sections 12142 and 12144, respectively?

(Testimony of David E. Watkins.)

A. I am.

Mr. Licking: What is the materiality? If the Court please, I object. What materiality has it if the witness is familiar with the laws of the State of California, or otherwise?

Mr. Deibert: Well, there are certain services enumerated which may be rendered by such clubs.

Mr. Licking: The law sets out the services.

Mr. Deibert: Yes, but some of them are not performed by this association.

The Court: Well, there may be vice in the question that [50] follows, but this is purely preliminary.

Mr. Licking: Well, his familiarity with it is entirely immaterial as to the law.

The Court: Well, preliminarily I will permit it.

Mr. Deibert: Q. Are you familiar with Section 12145 to 12156 of that Code? A. I am.

Mr. Licking: The same objection, if the Court please.

The Court: The same ruling.

Mr. Deibert: Q. Which of the services enumerated in Sections 12145 to 12156, inclusive, has your association rendered during the years 1935 down to the present time?

Mr. Licking: The question is slightly leading, but—

A. Tow service, emergency road service, map service, bail bond service, touring service, claim adjustment service, license service, and also a limited personal accident service insurance policy.

(Testimony of David E. Watkins.)

Mr. Deibert: Q. What was the type of your corporation as originally organized?

A. As a non-profit organization, with no stock.

Q. With no stock? A. How?

Q. No stock?

Mr. Licking: If the Court please, that is all in the articles of incorporation.

The Court: Yes. It is calling for a legal conclusion of [51] the witness, also.

Mr. Deibert: Q. Has there ever been any change in the type of your corporation as originally organized? A. No.

Mr. Licking: If the Court please—

Mr. Deibert: Explain the purpose of the association since you became secretary and general manager in 1913?

Mr. Licking: I object to that. The purpose of the organization is immaterial.

The Court: Oh, yes. I think you can go into the services it renders.

Mr. Deibert: Very well.

Q. What services has the club rendered during that period? A. The ones enumerated.

Mr. Licking: The witness just answered that question, if the Court please.

The Court: I suppose the purpose is to render those services.

Mr. Deibert: Well, there has been some slight change, your Honor, over the period of years, in the rendition of the—

The Court: You might ask him the question. what changes were made.

(Testimony of David E. Watkins.)

Mr. Deibert: Yes.

Q. Were certain services rendered in 1943 and 1944 during [52] the war period which were not rendered at other times?

A. Yes. The bail bond service, particularly.

Q. Well, what if any services were rendered in connection with the war effort?

A. Well, practically the Government had entree to all our services. We not only erected all the various signs like the Dim Out—

The Court: Can you stipulate that this witness' testimony would be the same or similar to that of the other witnesses in that respect, Mr. Licking?

Mr. Licking: I can stipulate to that very readily—

Mr. Deibert: With reference to the services rendered?

The Court: Yes, the additional services which were gone into quite copiously by Mr. Kahn.

Mr. Deibert: Yes, I think your Honor is right about that. If it may be stipulated that, with certain exceptions, however, about which Mr. Watkins is peculiarly—or with which he is peculiarly familiar.

The Court: Well, direct your attention—

Mr. Licking: What is there that Mr. Watkins knows that the other witness does not?

Mr. Deibert: Well, there are several things.

Mr. Licking: I won't object to a leading question if you go into those things.

Mr. Deibert: Q. What was the condition of the

(Testimony of David E. Watkins.)

highways in 1913, and in the early days of your association's existence? [53]

Mr. Licking: To which I object on the ground it is immaterial.

The Court: Overruled.

A. Well, as compared to today, they were deplorable in the West, and the only hard-surface roads used were in the cities. One of my first activities in 1914—

Mr. Licking: If the Court please, this does not even answer the question. I doubt if it is material in the first place, but this is not even answering the question. The condition of the highways in 1913 I will stipulate they were materially poorer than they are now.

A. Materially so, even in the cities.

The Court: I am interested in what was done in the association, if there was anything done in rendering service to the members in addition to those which have been testified to.

Mr. Licking: Yes.

Mr. Deibert: That is what I am trying to show, your Honor. This is a preliminary question.

Mr. Licking: What was done in 1913 and now has very little relevancy. We are concerned about a refund of a tax assessed in 1943 and 1944.

The Court: Well, possibly the history of the plaintiff will give us some index as to the services which were rendered during the tax year period in question. [54]

Mr. Deibert: We believe it is quite relevant for this reason, your Honor—

(Testimony of David E. Watkins.)

The Court: I have ruled in your favor.

Mr. Deibert: Will you answer the question?

A. What was the question?

Mr. Deibert: Will you read the question, Mr. Reporter?

(The reporter read as follows:

“Q. What was the condition of the highways in 1913, and in the early days of your association's existence?

A. Well, as compared to today they were deplorable in the West, and the only hard-surfaced roads used were in the cities. One of my first activities in 1914—”)

The Court: Restrict your answer to the services rendered by the association in remedying those conditions.

A. The association at that time appeared before various Governmental bodies. One of my first duties in 1914 was to appear before the city trustees of Mayfield, which is now part of Palo Alto, to have their main street, which is now 101, taken care of so in wet weather we could get through it.

The mountain roads in those days were like others with which we are all familiar, particularly the lake district and into Yosemite Valley, and they were in such condition that the association maintained tow trucks on the Big Oak Flat Road, the road into Tahoe on the other side—I forget the name of that grade near Placerville—all season, and likewise [55] on the Mariposa road. We even went into raising subscriptions to improve some of

(Testimony of David E. Watkins.)

these roads. Particularly I have in mind the Mariposa road, where at one meeting there were something like 2500. I am only mentioning that to show you the condition of the roads as they were then, compared with how we find them today.

Mr. Deibert: Q. What geographical area does your association serve?

A. The 45 northern counties of California and Northern Nevada.

Q. Was the same area served in 1943 and 1944?

A. It was.

Q. Are you familiar with the various activities of the plaintiff during the years 1943 and 1944, as well as other periods since you became secretary and general manager in 1913?

A. I am.

Q. Did you have any part in planning or establishing such activities?

A. Yes.

Q. What did you do in that connection?

Mr. Licking: To which I object as immaterial, as to what he had to do in establishing activities.

The Court: Overruled. What he did, is that your question?

Mr. Deibert: Yes, what he did.

A. Well, in my position, as I stated before, I had a much more [56] direct contact, and naturally, with the membership than the board of directors, not only in supervising the placing into execution of their various policies, but to go before them with possibly new policies, of which there were many during 1943 and 1944, with certain recommendations.

(Testimony of David E. Watkins.)

Mr. Licking: If the Court please, I move to strike that out as not responsive. It did not have anything to do with the question. He was asked what he did, and he has been talking about something else entirely.

The Court: I think it is responsive. Denied.

Mr. Deibert: Q. What were the activities of the plaintiff in the years 1943 and 1944 that were different from the other period?

Mr. Licking: Prior or subsequent?

Mr. Deibert: Prior and subsequent.

A. In 1943 and 1944 we had no finance department; we eliminated that prior to then; and neither did we have bail bond service. I don't know that there are any others that we eliminated. Of course, all our services during the war period were tremendously restricted through gasoline rationing and maintaining member services, such as emergency aid for touring, et cetera.

Q. Did you have to do more with the War and Navy Departments during the war period—

The Court: I understood counsel to stipulate the evidence would give in that regard as to the changes would be substantially [57] the same as Mr. Kahn's testimony, is that correct?

Mr. Deibert: Yes, your Honor.

Q. To whom were services of that nature rendered?

A. The members of the association.

Q. In your affidavit of November 5, 1941, Mr. Watkins, which is in Exhibit 1, there is in-

(Testimony of David E. Watkins.)

cluded on page 5, paragraph 8, Finance Department.

Mr. Licking: That is 1-D.

Mr. Deibert: 1-D, I think that is correct.

Q. That is the Finance Department that you say was eliminated? A. That is right.

Q. When?

A. I think it was—I wouldn't be positive on this, but it was February, I think, in 1942.

Q. In other words, you didn't have it in 1943 and 1944? A. No.

Q. Did you have any such—

A. I am not positive, but it was February, 1942.

Q. Have you had any such department since 1944? A. No.

Q. How many members did the association have on December 31, 1942? A. 104,352.

Q. On December 31, 1943? A. 108,601.

Q. On December 31, 1944? A. 116,929.

Q. Has your association received any letters since January 1, 1945, from the Commissioner of Internal Revenue, other than those included in the documents already stipulated in evidence, ruling on the question of your tax exempt status?

A. Well, I don't know which ones were stipulated—but no, I would answer that from my knowledge of them.

Q. Well, I show you—

Mr. Licking: May I see it?

Mr. Deibert: Certainly (exhibiting document to Mr. Licking).

(Testimony of David E. Watkins.)

Mr. Licking: These letters, if relevant, speak for themselves. There is no necessity of asking this witness about them. You can identify them. That is his signature, the deputy commissioner.

Mr. Deibert: Yes. Have you any objection to the introduction?

Mr. Licking: Yes. I don't see what they have to do with the case at all.

Mr. Deibert: Q. I hand you these letters—

Mr. Licking: I doubt if this witness can establish anything more than appears in the letters. The court can rule on the admissibility of the documents, but I don't see what the witness can do with them.

Mr. Deibert: These are letters I wish to present. [59]

Q. Do you recognize these letters?

Mr. Licking: I will stipulate that the letters were sent and received.

Mr. Deibert: Very well. I offer them in evidence, your Honor, as containing rulings by the Commissioner of Internal Revenue, in connection with the primary ruling in this case that the plaintiff in the case is an exempt organization. These letters refer to the rulings in some of the other letters which are already in evidence. For instance, the first one—

Mr. Licking: The letters, themselves, have to do with the capital stock tax. They haven't a thing to do with income taxes.

Mr. Deibert: They have to do with the capital

(Testimony of David E. Watkins.)

stock taxes, but they also refer to the other ruling of the Bureau, and they say further in this letter of January 25, 1945:

“In Bureau letter of December 23, 1944”—which is in the stipulation—“you were advised that you are not entitled to exemption from filing income tax returns under Section 101 of the Internal Revenue Code and the corresponding provisions of prior Revenue Acts. However, in order to avoid undue hardship, it has been held, under the authority granted by Section 3791(b) of the Code, that automobile clubs such as yours, which are within the scope of the Bureau rulings, will not be required to file returns of income for years prior to January 1, [60] 1943.”

The letter of the Commissioner of September 23—

Mr. Licking: What is the difference between that and the Commissioner's ruling?

Mr. Deibert: Well, the point is that the letters deny the application for refund of capital stock taxes, but tie up with the ruling in the letter of September 23, and they also recognize the fact that this association is a club—

Mr. Licking: Well, if the Court please—

The Court: Well, do they recognize it is a club within the meaning of this section 101 (9) of the Revenue Act?

Mr. Deibert: Yes.

Mr. Licking: The letters, if the Court please.

(Testimony of David E. Watkins.)

are for the purpose of this particular tax, the capital stock tax, and have nothing to do with income taxes.

The Court: Well, I am going to receive them.

Mr. Licking: Well, may I have an exception?

The Court: And I will consider the materiality after I read them.

Mr. Licking: May they be deemed read in the record?

The Court: Yes.

The Clerk: Do you want them as one exhibit?

Mr. Licking: May I have copies of them, Counsel?

Mr. Deibert: Pardon me?

Mr. Licking: Did you make copies of them? [61]

Mr. Deibert: Yes, I have copies, and if I may be permitted I would like to submit photostatic copies instead of the originals, and there is a set there for you—I think there are two sets there.

Mr. Licking: Let's get them in the record.

The Court: Do you offer these for any purpose other than to show the administrative interpretation?

Mr. Deibert: That is primarily the purpose, your Honor, yes, although they have a bearing on the former ruling, and the Bureau has ruled now that for income and capital stock tax purposes they are—

The Court: That is the only purpose, then, to show the administrative interpretation?

Mr. Deibert: Yes, your Honor.

(Testimony of David E. Watkins.)

The Clerk: How do you want these marked?

Mr. Licking: What is the exhibit number next in order?

The Clerk: No. 2.

Mr. Licking: Make this 2-A.

Mr. Deibert: 2-A, 2-B, and 2-C.

(The documents referred to were marked

Plaintiff's Exhibits 2-A, 2-B, and 2-C.)

Mr. Licking: 2-A is the letter of January 25, 1945.

Mr. Deibert: That is right.

Mr. Licking: And 2-B is the letter of February 23, 1945.

Mr. Deibert: Yes. [62]

Mr. Licking: And 2-C is the letter of August 21, 1945.

Mr. Deibert: That is right.

Mr. Licking: May I reserve an exception to the ruling?

Mr. Deibert: Q. Did your association ever pay any Federal income taxes for any year prior to those paid for the year 1943? A. No.

Q. Was your association ever called upon by the Federal Government to pay any income taxes for any year prior to those paid for the year 1943?

A. No.

Q. What services does your emergency road service department render?

Mr. Licking: If the Court please, we went into this with the other witnesses. It seems to me this is just cumulative.

(Testimony of David E. Watkins.)

Mr. Deibert: Your Honor, this is our position, if I may explain it: Mr. Kahn was president of the association in 1943 and 1944. He had also been a vice president and been a treasurer in earlier years, but he was never intimately—

The Court: I don't think there is a person in this room disputes the other witnesses that that road service is rendered. I think we are all conversant with it. I am quite sure Mr. Licking is conversant with it. It seems to me we are just taking time on something we all know exists.

Mr. Licking: The activities of the club are almost such [63] that on those matters—as a legal proposition I don't suppose the court can take judicial notice of them, but as a practical proposition—

The Court: I don't think you need more than one witness to prove it.

Mr. Deibert: We don't want to cumulate testimony, but—

The Court: Well, a matter like this that won't be controverted does not take corroboration, I don't think.

Mr. Deibert: Well, if that is your Honor's ruling —

The Court: Well: I don't want to be arbitrary about it, counsel, but I think that you are unnecessarily taking the time of the court and everybody to further pursue this line.

Mr. Deibert: May I ask just a few questions that were not answered by Mr. Kahn?

(Testimony of David E. Watkins.)

The Court: You may.

Mr. Deibert: Q. What type of automobiles belonging to members are eligible for emergency road service? A. Passenger cars.

Q. What amount of money did your association pay to commercial garages in your territory for emergency road service in 1943?

Mr. Licking: What is the materiality of that, Counsel?

The Court: Showing the services rendered.

A. In 1943 we paid \$199,325.

Q. In 1944? A. \$262,017. [64]

Mr. Licking: Doesn't that show on the statements that are already in evidence, Counsel?

Mr. Deibert: No, no it does not.

Q. When did your association begin the erection, maintenance and repair of signs on places of historical interest in your territory?

A. In 1914.

Q. Had any other organization done that work before you began it?

A. The Goodrich Tire Company had signs scattered, but they weren't standard—they were standardized, too, but they did not cover the roads and many of the mountain areas and so forth. No other extensively, to my knowledge.

Q. To your knowledge has any other individual or organization done any such work since the organization began to do it? A. No.

Q. What was the purpose of your association beginning and continuing this work over the years?

(Testimony of David E. Watkins.)

A. Well, for the recreational convenience and pelasure of our members.

Mr. Licking: That is objected to on the ground it calls for a conclusion of the witness.

A. We even went so far—on the El Camino Real in directing to the Missions — this was, I think, in 1914 or 1915—you still see many of them on the highways, the old Mission bell, and the first road starting, we marked the telephone poles between [65] Los Angeles and San Francisco—"L. A.", with an arrow pointing to Los Angeles, and "San Francisco" on the telephone poles, and from that the next step was the directors decided that a single agency to cover all county roads, municipal streets and State highways would add much to the comfort of our membership, and particularly in the mountain areas. In the mountain areas, usually in those days when you came to a fork of the road a sign meant something, and they recognized with all our resorts, where vacations and all were planned, that it would make a decided hit, so to speak, with the membership, and those are the real reasons why we went into the signing work.

Q. Is there any other organization or individual, to your knowledge, in California to furnish or does furnish information and services of the same scope as your association within your territory?

A. No.

Q. Was there, in 1933 or 1934?

A. No.

Q. Has your association, since your employment

(Testimony of David E. Watkins.)

in 1913, made efforts to obtain either favorable or restrictive legislation from the legislature?

A. Definitely, yes.

Q. Has it done any of that work with municipalities or counties?

A. Yes.

Q. What has been the result of that work?

A. Well—

Mr. Licking: If the Court please—

A. —from a State standpoint—

Mr. Licking: —it seems to me this is entirely immaterial. I don't see what it proves, how it touches any issue in the case, and it is purely a conclusion as to what has been established.

The Court: It seems to me that is immaterial. The service rendered is one thing, and whether it is effective or not would make no difference if an attempt was made to benefit the members in some way. The service is there whether it is successful or unsuccessful.

Mr. Deibert: Wouldn't it go to the efficiency of the service rendered, your Honor?

The Court: That would not necessarily follow.

Mr. Licking: If the Court please, I am perfectly willing to stipulate their services are efficient if you consider that relevant.

The Court: Pardon me?

Mr. Licking: I am perfectly willing to stipulate that the services that are rendered for the amount paid by the members are efficient. I don't think there is any question about that. It seems to me that for the sum of \$15 a year the first year, and

(Testimony of David E. Watkins.)

\$12 a year after that, for the services that have been enumerated here—they are very efficient in supplying [67] those services for that amount of money.

The Court: Does that suffice?

Mr. Deibert: Yes, your Honor, with that stipulation we will accept it.

Q. When was your licensing department established? A. In 1924.

Q. Was it in operation during 1943 and 1944?

A. Yes.

Q. What was the purpose of organizing that department?

A. For the convenience and pleasure of our members, and preventing them from waiting during the registration period to get these services.

Q. What functions does that department perform?

A. Well, they issue the original license plates to the members, and a block is assigned to us by the State, and those are given promptly to the members. We handle all the transfers of ownership and practically everything coming up under the Motor Vehicle Department with the exception of issuing operators' cards.

Q. Is this service extended to anyone other than members of the association? A. It is not.

Q. Does any net income come to the association from the operation of this department?

A. No, sir. [68]

Q. What services is rendered to your members by the adjustment and traffic department?

(Testimony of David E. Watkins.)

A. By the which?

Q. The adjustment and traffic department.

A. Well—

Mr. Licking: That has been discussed by the other witnesses.

The Court: Hasn't it been sufficiently described?

Mr. Deibert: Well, perhaps it has been, your Honor.

The Court: Unless you want to go into the question of legal services again.

Mr. Deibert: No, we have no such desire.

A. In a way—I heard Mr. Kahn's testimony this morning on this department—

Q. Is there anything you can add to it?

A. I can definitely add we do not represent members in court. I don't know that that was made clear this morning. In adjustments we represent them, which is all in agreement with the State Bar Association. We have had that agreement now for several years.

The Court: I am afraid we are getting into the subject of legal services again.

Mr. Licking: I am not amending my remarks in any way, but I don't see anything that could be considered that the association was engaged in the practice of law. [69]

The Court: I am glad that is eliminated from the case.

Mr. Deibert: Q. Do you publish a monthly magazine? A. Yes, sir.

Q. Did you publish that monthly in 1943 and

(Testimony of David E. Watkins.)

1944? A. Yes, sir.

Q. What was the name of the magazine?

A. Motorland.

Q. What was the cost of the publication in 1943? A. \$45,102.

Q. In 1944? A. \$47,050.

Q. Did you have any income from advertising in the magazine in 1943? A. No, sir.

Q. Or 1944? A. No, sir.

Q. Did income from advertising in the magazine cease after you had made your affidavit of October 5, 1941, which is part of Exhibit 1?

Mr. Licking: Just one moment—

Mr. Deibert: Reference is made in that affidavit to income from advertising, your Honor, and I simply want to establish that after that affidavit that was abandoned.

The Court: When was that abandoned?

Mr. Licking: That is 1-D. [70]

A. It was abandoned—I am not definitely sure on that—in 1941—

Mr. Licking: Counsel, again I make the offer; I haven't any objection to leading questions. If you take this exhibit, which is 1-D, and ask the witness a leading question as to the different activities I have no objection. The court has ruled, as I understand the court's ruling, that the witness' testimony is not material or relevant, except as to whatever conditions there are in his affidavit that the other witnesses have not testified to. I haven't any objection to a leading question if there are any other differences.

(Testimony of David E. Watkins.)

Mr. Deibert: I cannot concede that is a leading question, Mr. Licking; I am simply asking for the fact.

A. It was abandoned in 1941; the exact date I don't know.

Q. Why did you discontinue carrying any paid advertising in the magazine? A. When?

Q. Why.

Mr. Licking: I object to that on the ground it is immaterial why.

The Court: I don't see any materiality in it.

Mr. Deibert: Q. What was the circulation of the magazine in 1943?

Mr. Licking: That is immaterial, if the Court please.

The Court: If it is supplied to the members—

Mr. Deibert: That is what I am leading up to, your Honor.

The Court: Overruled.

A. 108,000 in 1943, and 114,000—that is, per month, in 1944.

Mr. Licking: That is to all of the members. Those figures seem familiar, if it is issued to each member.

Mr. Deibert: I am just about to ask that question.

Q. To whom is the magazine distributed?

A. To the membership of the club.

Q. What was the purpose of beginning the publication of such a magazine?

Mr. Licking: Object to the purpose, if the Court please.

(Testimony of David E. Watkins.)

Mr. Deibert: It seems to me that shows the beginning of one of the activities—

The Court: Overruled.

A. It was to keep our membership advised, not only of the activities of the association, but of all matters of interest arising in connection with the operation of their automobiles.

Mr. Deibert: Q. Did it have the same purposes in 1943 and 1944? A. Yes, sir.

Q. When was the magazine first published?

A. In 1917, as the California Motorist.

Q. Was the name changed later?

A. In 1919, to Motorland.

Q. Has it always been distributed as published to the entire [72] membership of the association?

A. Yes, sir.

Q. Is it still published and distributed to the members monthly? A. Yes, sir.

Q. Is it sold on news stands or otherwise to the general public? A. No, sir.

Q. Does it now have any income from advertising? A. No, sir.

Q. Did your association in 1943 or 1944 issue any memberships other than to individuals?

A. No, sir.

Q. Do you issue memberships to operators of trucks or other commercial motor vehicles?

A. No, sir.

Q. Have you ever done so? A. No, sir.

Q. Has your association ever rented any of its properties to tenants? A. Yes, sir.

(Testimony of David E. Watkins.)

Q. When?

A. When we moved into our new building here that we now occupy.

Mr. Licking: If the Court please, it seems to me that the activities should be confined to the time involved, not what they once did, but what they subsequently did. [73]

Mr. Deibert: We have stated in Mr. Watkins' affidavit of November 5, 1941—there was a statement that there was income of \$125 per month from a garage, and I am developing now that that was abandoned later on.

Mr. Licking: Why not ask the direct question? I have no objection to that.

Mr. Deibert: I didn't want to ask a leading question.

Mr. Licking: I said I have no objection; I would waive that just to save time.

Mr. Deibert: Very well.

Q. Did you ever rent a garage in connection with your property? A. Yes.

Q. What monthly rental?

A. Well, in later years, \$125 a month, at least that. It was more—

Q. When did you start renting that garage?

A. In October, 1941.

Q. Why did you stop renting it?

Mr. Licking: We object. What difference does it make?

The Court: Sustained.

Mr. Licking: It is immaterial why they stopped renting it.

(Testimony of David E. Watkins.)

The Court: Sustained.

Mr. Deibert: Q. Did you derive any profit from the rental of any property in 1943 and 1944?

Mr. Licking: To which I object. It calls for a conclusion [74] of the witness, was there any property rented. The question is, did you derive any profit?

Mr. Deibert: Very well.

Q. Did you derive any profit from rentals in 1943 and 1944?

The Court: Q. Did you rent any property?

The Witness: A. No, unless you construed—we didn't rent it. The Army took the sixth floor part of it by force and after a length of time they gave us twelve hundred dollars, I think, and that is all. Nothing outside of that.

Mr. Deibert: Q. Was it commandeered?

A. What?

Q. Was it commandeered?

A. Yes, definitely so.

Mr. Licking: What do you mean by "commandeered"?

Mr. Deibert: Q. Was it rented voluntarily or at your solicitation, or did the Army come in and say they wanted it?

A. They came in and told us they were going to take it, and we said, "Fine."

Q. What was the fee for new members in 1943 and 1944?

A. Annual dues of \$12, and the new member, \$15.

(Testimony of David E. Watkins.)

Q. What did the other three dollars mean?

A. That was enrollment fee or initiation fee.

Mr. Licking: That has all been testified to by the other witness.

Mr. Deibert: Q. Were there any memberships in your [75] Association other than those of individuals in 1943 and 1944? A. No.

Mr. Licking: The question has been asked and answered of this witness. He has already said they were not.

The Court: Overruled.

Mr. Deibert: Q. Was there any such membership since 1944? A. No.

Q. What amount of income was derived from such memberships in 1943, from members in 1943?

Mr. Licking: If the Court please, isn't that in the record already, in the statements?

Mr. Deibert: No, I beg your pardon, it is not, Mr. Licking. If it were I wouldn't ask that.

Mr. Licking: The income from memberships?

Mr. Deibert: No, not in the record.

A. I don't have that figure, but it is over a million dollars, a million three hundred, I think, in 1943, and a little more in 1944.

Q. Was it necessary for a hotel, garage or service station to take out a membership in the Association in order to be listed in the Association's guidebooks or lists of approved facilities?

A. When?

Q. In 1943 and 1944? A. No. [76]

Q. How were lists of such approved places of business obtained?

(Testimony of David E. Watkins.)

A. By our own employees through making inspections, which, of course, qualified them for the respective divisions that we set up, one-star, two-star and three-star.

Q. What was the purpose of approving and listing such places?

Mr. Licking: The fact that the witness just testified to, if the Court please, is in Exhibit 1-H, the income for that year, income tax returns.

The Court: You mean the income from members?

Mr. Licking: The income from members.

Mr. Deibert: I beg your pardon, your Honor. I had forgotten for the moment that we had introduced in the stipulation the income tax returns. I beg your pardon.

A. What was the question?

Q. What was the purpose of approving and listing such places?

A. Naturally it was for the convenience and comfort and pleasure of our members, particularly. We displayed a sign in front of each place when travelling through observation of the sign they would know the type of place it was.

Q. Did the sign so indicate?

A. Yes. We had ratings, one, two and three stars. One designating the luxurious types, like the St. Francis and the Palace, for example; No. 2, the less luxurious type, like the Stewart here in town. for example, and No. 3 was the [77] lesser types where accommodations could be had and it was a good clean hotel.

(Testimony of David E. Watkins.)

Q. What amount did your Association expend in 1943 for road-signing materials?

A. For the materials?

Q. Yes? A. In 1943, \$35,602.

Q. In 1944? A. \$33,735.

Q. Was the Association reimbursed in full for the cost of such materials?

A. Never received anything — the various branches of Government paid for that—but the Association bought them, naturally, and it was reimbursed by the various branches of government.

Q. That was my question. That is, you mean the State Government?

A. State, municipalities, federal and counties.

Q. Was there any element of profit in the purchase and use of such materials to your Association? A. No, sir.

Q. What amount did the Association expend in 1943 for erecting and maintaining road signs?

A. In 1943, \$98,005.

Q. In 1944? [78] A. In 1944, \$104,656.

Mr. Licking: That is all, if the Court please, over all of these years in the exhibits.

The Court: If it is, I see no occasion to go into it further.

Mr. Licking: I don't know what the purpose is.

Mr. Deibert: Well, these are not in the detail, your Honor, that I wanted to bring out by interrogation.

Mr. Licking: May I ask what is the materiality if there was \$54 or \$54,000 spent? What materiality is there?

(Testimony of David E. Watkins.)

Mr. Deibert: Well, we want to show how the money of the Association was spent.

The Court: I think that is proper.

Mr. Licking: But, if the Court please, the Association for this period has filed a detailed income tax return showing where they got the money and what they did with it.

The Court: If the details are in that, I see no purpose in going into it, but Counsel says it is not there.

Mr. Licking: Well, in this instance I have gone down there and found the exact figures.

Mr. Deibert: Q. Was the Association ever reimbursed by anyone latter expenses, that is, the labor expenditures? A. No.

Q. In 1943 and 1944? A. No. [79]

Q. What was the reason the Association made these expenditures without reimbursement?

Mr. Licking: If the Court please, that is immaterial, it seems to me, and calls for a self-serving declaration on the part of an officer of the corporation.

Mr. Deibert: It seems to me it is one of the services rendered by the Association, and that is one of the definite elements in this case.

Mr. Licking: Your question was not with reference to services, it was why did you do it. That is what your question was in effect, "Why did you do it?"

Mr. Deibert: Yes, what was the reason the Association made the expenditures without reimbursement? Why didn't they ask somebody to pay?

(Testimony of David E. Watkins.)

The Court: What difference does it make?

Mr. Deibert: It seems to me that the answer would bring out, your Honor, that this is one of the services which the Association historically has always rendered to its membership.

Mr. Licking: Well, that has been brought out, and I suggest it will come up afterwards in argument.

The Court: The picture is clear it was expended undoubtedly with the expectation of reimbursement by the political agencies.

Mr. Deibert: The point is this, your Honor, that the [80] road-signing materials, that is, the materials themselves the Association was reimbursed for by the State, counties, cities and smaller municipalities, but for the labor expended they were not.

Mr. Licking: That is stipulated. There is no question about that.

The Court: Yes.

Mr. Deibert: Q. Did the Association have any other income from other sources in 1943 and 1944?

Mr. Licking: Well, if the Court please, the source of income—they have filed an income tax return. It is all there.

Mr. Deibert: Very well, I will withdraw the question.

Q. What disposition is made of the annual income by the Association? A. Made of what?

Q. Of the annual income?

Mr. Licking: That question is answered by the statements that are filed.

(Testimony of David E. Watkins.)

The Court: Doesn't that answer it?

Mr. Deibert: Well, it is answered in so many figures, your Honor—

The Court: Well, not only the figures, but it is broken down as to the classification of expenditures.

Mr. Deibert: That is true. There are certain highlights, [81] however, I think, that have a pertinency.

The Court: Well, Counsel is not objecting to leading questions. If there is anything you want in the way of amplification of this item of expenditure, put your leading question.

Mr. Deibert: Well, that was just a general question.

The Court: Well, the general question is answered by this exhibit.

Mr. Deibert: To a large degree it is, yes, I agree with your Honor.

The Court: If you want to amplify it, you can ask leading questions.

Mr. Deibert: Q. Is there any way you want to amplify the list attached to the income tax returns, Mr. Watkins, as to your—as to the disposition of your annual income?

A. No. Our annual income is given and it has always been the policy to expend this money for services. Now, in 1943 and 1944 our services were definitely restricted. Through gasoline rationing we had to cut down emergency first aid, et cetera.

Mr. Licking: If the Court please, this witness

(Testimony of David E. Watkins.)

has made that identical statement now several times, and I am perfectly willing to stipulate their services were curtailed during the war years.

Mr. Deibert: Very well. [82]

Q. Has your Association ever paid dividends of any nature to any member? A. No.

Q. Has any income of your Association ever inured to the benefit of any member of the Association?

Mr. Licking: That calls for a conclusion of the witness.

The Court: Sustained.

Mr. Deibert: Q. Let me ask you this: Has any income of the Association ever been paid or credited to any member on your books? A. No.

Q. And have any provisions ever been made to pay or to credit any net earnings of the Association to these members? A. No.

Q. Has the Association any plan or purpose to distribute its net earnings so as to inure to the benefit of any individual member? A. No.

Q. Does any director of the Association receive any salary or other compensation? A. No.

Q. Did any officer as such receive any salary or other compensation in 1943 and 1944?

A. No.

Q. Has your Association at any time engaged in or made any [83] arrangement for its members to participate in any deal whereby members could obtain discounts on supplies or services of any character? A. No.

(Testimony of David E. Watkins.)

Q. Has it ever been a plan or policy of the Association to attempt to obtain any such discount for its members?

A. State that question again?

Q. Has it ever been the plan or policy of the Association to attempt to obtain any such discount?

A. No, no.

Q. Has your Association ever financed or helped to finance the purchase of automobiles by your members or anyone else? A. No.

Mr. Licking: If the Court please, what they did not do, it seems to me is not relevant. I can't see what the materiality of these questions, "You didn't do so and so".

The Court: I think so.

Mr. Deibert: I beg your pardon. If your Honor will read, as you probably will do later, this G.C.M., as it is called—General Counsel Memorandum issued by the Internal Revenue Bureau, on which the ruling in this case is based, you will observe in there mention that certain members of automobile associations have obtained discounts on the services rendered on behalf of their memberships. Now, it seems to me we should not be attacked by the Bureau on the [84] ground that we come within the purview of that ruling of the Commissioner of Internal Revenue without having any chance to explain that we do not do these same things.

Mr. Licking: If the Court please, the statement Mr. Deibert makes would illustrate that it is just what it is, it is argumentative. It hasn't any evi-

(Testimony of David E. Watkins.)

dentiary value; it shows nothing to the Court at all. It is merely argumentative. He can distinguish the Commissioner's ruling, I take it, but the time to do that is in the briefs and not with the help of this witness, whose testimony has been entirely a question of "I didn't do this and I didn't do that".

The Court: You have a peculiar situation here, that of determining the character of an organization, and I suppose the character of an organization is determined not only by what the organization does, but by what it does not do.

Mr. Licking: I am perfectly willing to stipulate, if your Honor feels it is necessary, that the Association here, as far as I know, did everything that is in the record here that they did do and did nothing else.

Now, to accentuate the things that they did not do is just argumentative. It seems to me there is utterly no sense to it.

Mr. Deibert: It seems to me, your Honor, we should be entitled to show what we did not do as well as what we did in order to show we do not come within the purview of that ruling. [85]

The Court: That is all right, if you want to go into that. Overruled.

Mr. Deibert: That is the purpose of going into it.

The Court: I understood Counsel to say he would stipulate—

Mr. Licking: I said I would stipulate they did

(Testimony of David E. Watkins.)

not do anything except what the record shows they did that is in evidence here.

The Court: I should think that would be sufficient.

Mr. Deibert: Very well, your Honor.

Q. Does your Association have a Board of Directors? A. Yes, sir.

Q. Has it always had such a board?

A. Yes.

Mr. Licking: Well, if the Court please, the articles of incorporation and bylaws and everything else of the Association are here, they are in evidence, and they are still operating under those.

The Court: Mr. Kahn so testified also. It is a matter that is not in dispute, apparently.

Mr. Deibert: Has the Board ever held meetings outside of its headquarters in San Francisco?

A. Yes.

Mr. Licking: What difference does that make? That is immaterial. [86]

Mr. Deibert: It makes quite a difference to us, Mr. Licking. We have been charged by the Bureau of Internal Revenue as not being a club organized within the purview of Section 101(9) because there was no commingling of members. That is one of the bases of the Bureau's ruling, and it seems to me, your Honor, we should be permitted to point out that those facts do not apply to our organization.

The Court: Go ahead.

Mr. Deibert: Will you read the question, Mr. Reporter?

(Testimony of David E. Watkins.)

The Court: Q. Did you have meetings of the Board of Directors outside of San Francisco?

The Witness: A. Yes, yes.

Mr. Deibert: For what purpose?

A. Well, before the membership grew to such proportions, we used to hold board meetings in the various districts and invite the membership in those districts in; but, as stated, the growth of the membership in recent years has prohibited such procedure.

Q. How many members are there on your Board of Directors? A. 21.

Q. How many were there during 1943 and 1944?

A. 21.

Q. Were all members of the Board members of the Association in those years?

A. Yes, sir. [87]

Q. Does the Board have regular times for meeting? A. Yes, sir.

Q. What are the times for meeting?

Mr. Licking: Isn't that in evidence?

A. The fourth Friday of every month.

Mr. Licking: Isn't that in evidence, Counsel?

Mr. Deibert: This goes to the question of whether or not the members ever get together for any purpose, and that is one of the fundamental bases for the Bureau's so-called adverse ruling.

A. The fourth Friday of every month.

Mr. Deibert: Q. Were special meetings of the Board ever held? A. Yes.

Q. Were there any such special meetings in 1943 and 1944? A. I don't recall.

(Testimony of David E. Watkins.)

Q. Did the members of the Board of Directors receive any compensation as such? A. No.

The Court: That was asked and answered.

Mr. Deibert: Pardon me?

The Court: That was asked and answered.

Mr. Deibert: Q. Are there any standing committees of the Association? A. Yes. [88]

Q. How many? A. Ten.

Q. Ten? A. Ten.

Q. Will you name them?

A. Finance Committee, E. B. Degold, Chairman—

The Court: We aren't interested in the chairman. The question is, what are the committees.

Mr. Licking: I will stipulate that a list of these be deemed read into the record and filed.

The Court: Do you have a list of them?

The Witness: A. Yes, it is a part of this. I can read them.

The Court: Read them.

The Witness: A. Public Safety Committee, Membership Committee, Good Roads Committee, Emergency Road Service Committee, Publicity Committee, Legislative Committee, Transcontinental Highway Committee, Forestry Committee and Executive Committee, with the chairman of each standing committee constituting the Executive Committee.

Mr. Deibert: Q. How many members does each of these committees have? A. Five.

Q. Were those the committees and the number of members on each such committee in 1943 and

(Testimony of David E. Watkins.)

1944? [89] A. They were.

Q. Do the members of the several committees receive any compensation as such members?

A. They do not.

Q. Can you describe briefly the duties and functions of each of these committees, are they contemplated in the name?

A. Well, they suggest the functions. They make studies of policy or activities, and then just before the meeting of the Board they meet and analyze them more thoroughly and go before the Board with their recommendations.

Q. When do the standing committees meet?

A. At the call of the chairman.

Q. Is there any contact, to your knowledge, or association between members of any of the committees between committee meetings?

A. Oh, definitely. If a subject comes up, particularly if it is of much importance—very frequently I happen to know of meetings of maybe a couple or three of them—particularly the ones residing, maybe, in San Francisco. The interior, no, unless they are in the city.

Q. Have the members of your Association the right to participate in the affairs of the Association?

A. Yes, sir.

Q. Did they have such right in 1943 and 1944?

A. Yes, sir. [90]

Q. Did they exercise such rights in 1943 and 1944?

A. Yes, sir.

Q. In what manner?

Mr. Licking: What was that question?

(Testimony of David E. Watkins.)

The Court: The participation of the members in these meetings.

Mr. Licking: I thought when I first heard it, it was a question of whether they did participate in the meetings or not. What was the question? Whether they had a right to or did participate?

The Court: No, did they participate.

Mr. Deibert: No, in what manner.

The Court: Nothing was said about right. Did they participate in such meetings?

Mr. Licking: The question is indefinite.

Mr. Deibert: Q. State in what manner did they participate.

Mr. Licking: In what, meetings?

Mr. Deibert: Well, in the affairs of the Association. That was the preliminary question.

Mr. Licking: The question is indefinite.

The Court: Let us see if the witness can make that definite by his answer. In what manner did they participate?

The Witness: A. In particular, in the annual board meetings. Notice is sent out at least sixty days, according to the constitution and bylaws, prior to the meeting, and they [91] are there expressing their views.

The Court: They are not all there?

The Witness: A. No, no. And we urge if they can't be present, in the notice, to name someone as their proxy, and we do have a great number of proxies.

Mr. Deibert: Q. And you send out such notices and proxies?

(Testimony of David E. Watkins.)

A. That is right, sixty days prior to the annual meeting.

Mr. Deibert: I should like to introduce in evidence, your Honor, a notice of annual meeting.

Mr. Licking: What difference does it make? There is one meeting a year in which the members may participate and express their views. That is one meeting a year.

Mr. Deibert: Q. Are there any other meetings in which the members have any voice?

A. They are not invited, but they are frequently in on special committee meetings like legislative. Members who are not a part of our board do sit in on those meetings.

Mr. Licking: They haven't any right to do so.

The Court: They are there by invitation?

The Witness: A. They are not barred, but if they express an interest in it, they are invited.

The Court: Q. But they don't get notice?

Mr. Licking: I am perfectly willing to stipulate they hold meetings every year in which the members can come to [92] if they want to and vote.

Mr. Deibert: This notice includes a form of proxy. I would like that in evidence.

Mr. Licking: No objection.

(The documents referred to were thereupon received in evidence and marked Plaintiff's Exhibit 3.)

Mr. Deibert: Q. Has your Association a federation of automobile clubs? Do you have any member clubs? A. No, sir.

(Testimony of David E. Watkins.)

Q. Did it in 1943 and 1944? A. No.

Mr. Licking: Didn't Mr. Kahn go over that identical ground?

Mr. Deibert: No, I beg your pardon, he did not.

Mr. Licking: About member clubs?

Mr. Deibert: No, I don't think he mentioned that.

Q. Has it ever managed local automobile clubs?

A. No.

Q. Did it have any member clubs in 1943 and 1944? A. No.

Q. To your knowledge, how many federations of automobile clubs are there in the United States?

Mr. Licking: Which, if the Court please, is immaterial. I don't see what difference it makes.

Mr. Deibert: I want to bring out the distinction—

The Court: You want to bring out the distinction between this Association and other automobile associations?

Mr. Deibert: Yes.

The Court: Overruled.

The Witness: A. The American Automobile Association is our affiliate, but affiliated with that likewise are approximately six hundred other clubs throughout the United States.

Mr. Deibert: Q. What agreement does your Association have with such other clubs for services?

A. We recognize their membership card practically the same as ours when they are visiting in our territory. They are entitled to our emergency road service, map service—in fact, the services of all our

(Testimony of David E. Watkins.)

departments the same as our members are when touring in their respective territories.

Q. Are you connected with the California State Automobile Association Inter-Insurance Bureau?

A. Yes.

Q. That is a part of your Association?

A. No.

Q. Are members of your Association required to become subscribers to the Inter-Insurance Bureau? A. No.

Q. Do your Association and the Inter-Insurance Bureau occupy the same office quarters in any locality? A. In San Francisco--yes. [94]

Q. Where?

A. Well, in San Francisco and all the thirty-five district offices.

Q. Does the Inter-Insurance Bureau compensate your Association for the space it occupies?

A. Yes.

Q. On what basis?

A. We had a survey made of the entire building, the various floors, and the rental upon a square foot basis was given us by these experts, and the Insurance Department pays the Association for the space it occupies upon those bases.

Q. Has your Association ever made any profit out of sharing the quarters with the Inter-Insurance Bureau? A. No, sir.

Q. Does the Inter-Insurance Bureau share any other expenses with your Association?

A. Yes, sir.

(Testimony of David E. Watkins.)

Q. On what basis?

A. What is the question?

Q. On what basis?

A. Well, we operate—we have thirty-five district offices, and surveys at different intervals are made—or, rather, preceding that, the same staff represents the insurance activities the same as the club, and with the thirty-five offices, you can understand that we could not split some managers to [95] do the adjusting, like at Yreka and Susanville, which are principally service organizations, whereas other offices like Oakland has, for instance, six adjusters. So we make a survey of all these different offices at intervals and ascertain what part of the time of the employee they require and what space they would naturally occupy in those buildings, and then we come to an agreement upon the proper percentage of the cost of those offices that should be borne by each.

Q. How is reimbursement made by the Inter-Insurance Bureau to your Association for their share of the cost?

A. Each month by check.

Q. Is any profit derived by your Association from sharing expenses of any nature with the Inter-Insurance Bureau?

A. No, sir.

Mr. Licking: If the Court please, whether or not profit is derived is a matter of opinion of the witness. The books are in evidence here.

The Court: Sustained.

Mr. Deibert: That is all. Take the witness.

The Court: We will take the afternoon recess.

(Recess.)

(Testimony of David E. Watkins.)

The Court: You may proceed.

Mr. Licking: You have finished?

Mr. Deibert: Yes. [96]

Cross Examination

Mr. Licking: Q. Mr. Watkins, is it your testimony that this insurance agency is something entirely separate, distinct and apart from your Association? A. That is right.

Q. And this insurance agency which is entirely separate, distinct and apart from your Association, occupies the same offices and utilizes the same personnel? That is correct, isn't it?

A. That latter part you said, occupies?

Q. Occupies the same offices and utilizes the same personnel?

A. That is right—the same personnel, I don't get that.

Q. I mean, one does a part of this work for the insurance company and a part of this work for the—

A. Through the district offices, that is right.

Q. Now, in several of your answers there, that a lot of people, directors and other people did not receive any salary as such, I notice referring to Exhibit 1-H and 1-I, that there is a pretty sizable amount set down for salaries. For instance, referring to Exhibit 1-H, there is some eighty-seven odd thousand dollars down there. It is on Page 3, your Honor, of the attached statement. Some \$97,522.07 set down for salary. A. For whom?

(Testimony of David E. Watkins.)

Q. That is just what I was going to ask you.

The Court: Is this 1943?

Mr. Licking: It is Exhibit 1-H, your Honor.

The Court: You say ninety-seven thousand. The one I have for 1943 shows 523,000. 97,000 refers to automobile expenses, if I have the same statement you have.

Mr. Licking: Well, I thought, your Honor, that the first—that the first column—I see, the first column runs across—the first column there to \$749,000. That is correct. I hadn't got the columns. I think your Honor's statement is correct. Paid salaries of some \$523,000.

The Court: I though I would correct you. You said \$97,000 was sizable.

Mr. Licking: Well, what I want to get at is, is any of these non-compensated directors or other officers in this salary statement? For instance, yourself. You are a director, I take it.

A. No, I am not.

Q. You are not? A. No.

Q. Well, are any of the directors also employees? A. Not a one.

Q. None of them?

A. In fact, there is a ruling—one of the first requests I made when we only had a few members was that I would never be called upon to hire a director or a friend or relative of [98] a director.

Q. In other words, directors are not paid any salary as such? A. They are not.

Q. I notice in your answer you said, "As such they were not."

(Testimony of David E. Watkins.)

A. I will say as such, or any other way.

The Court: Well, you had in mind the expense of attending meetings?

A. No. If they go back on a meeting—like if the club wants them they pay their expenses, that it true, but outside of that, definitely no.

Mr. Licking: Q. In other words, they are paid their expenses in attending meetings, but as far as salaries are concerned they receive none?

A. That is right.

Q. When you said, “as such,” you meant they received no salary at all?

A. They are not being compensated in any manner.

Q. Now, you heard Mr. Kahn’s testimony on the stand? You heard Mr. Kahn’s testimony?

A. Well, most of it, yes.

Q. And I take it you agree with Mr. Kahn that there is no social intercourse or social mingling in the club?

A. I have been thinking that over. How do you interpret social intermingling of the members?

Q. I mean intermingling of the members as a club function. I [99] take it the members occasionally speak to each other and visit each other’s houses, but outside of the annual meeting, you have no other—

A. Well, outside of our annual meetings and the various meetings I previously described, then I would say no.

Q. What are the various meetings you previously described?

(Testimony of David E. Watkins.)

A. In 1943 and 1944, no, outside of our annual meeting. Prior to that time, as I stated, we used to hold our directors' meeting over the district, and invite the members in. Then if that was a social activity, which I assume it was, there was that social feature.

Q. Came in to talk over the business?

A. That is right.

Q. I mean you didn't hold any dances or you didn't raffle anything—

A. No, but we all took a run into Yosemite the next day.

Q. Pardon me?

A. I was talking about the Merced meeting, we all took a run into Yosemite the next day, the members and directors and all.

Q. Was that as a club, that trip when you went to Yosemite?

A. No, we were all on our own, that is correct.
Mr. Licking: I think that is all.

Redirect Examination

Mr. Deibert: Q. You said, Mr. Watkins, in answer to Mr. Licking's question, you used the same personnel in your offices. [100] I understood you also to state that is true in the district offices, but is that true in the San Francisco office?

A. No. I thought I made that clear. I said that was true in the district offices, but not in the home office.

Q. Yes. I hand you a statement of income and expense, which constitutes a part of Exhibit 1, it

(Testimony of David E. Watkins.)

is a portion of the affidavit of Mr.—it is 1-D—it is an exhibit to 1-D, and I call your attention to the fact that the second item there, “Special Memberships, Hotels, Garages, et cetera,” for the years 1940 back to 1932 on that page—

Mr. Licking: Page 2?

Mr. Deibert: Pardon me?

Mr. Licking: What page?

Mr. Deibert: The first page of the exhibit.

A. The second line.

Mr. Deibert: Of the exhibit in the affidavit, the exhibit to the affidavit. The statement right there on your desk, Mr. Licking.

Q. And I ask you whether you had such special memberships in 1943 and 1944. A. No.

Mr. Deibert: That is all. Mr. James W. Johnson, will you take the stand? [101]

JAMES W. JOHNSON,

called as a witness on behalf of plaintiff; sworn.

Direct Examination

Mr. Deibert: Q. Where do you reside?

3. 2701 Van Ness Avenue.

Q. By whom are you now employed?

A. California State Automobile Association.

Q. In what capacity?

A. Chief engineer in charge of road signing and map-making.

Q. What is your business address?

A. 150 Van Ness Avenue, San Francisco.

(Testimony of James W. Johnson.)

Q. How long have you been employed by California State Automobile Association?

A. Since 1914.

Q. How long have you been chief engineer?

A. Since 1914.

Q. What are the functions of your road signing department?

A. The erection and maintenance—

Mr. Licking: If the Court please, they have asked this question now of two witnesses.

Mr. Deibert: There are certain details, your Honor, that I think this witness and only he can testify to.

Mr. Licking: What is the materiality of the details?

Mr. Deibert: Well, the details go to show what services were rendered to the members of the association, and that is one of the matters— [102]

The Court: Is there anything you can tell us that has not been testified to by the preceding two witnesses in reference to services rendered in the road signing department?

A. In general, I probably could not add to it, but in detail there is probably detail that I could.

Mr. Licking: What is the materiality of the details?

Mr. Deibert: The detail, your Honor, will show just exactly how the members were benefited by the erection and maintenance—

The Court: If there is anything you can add I will hear the witness.

(Testimony of James W. Johnson.)

Mr. Licking: How will this witness testify to how the members were benefited, if the Court please?

The Court: He can't very well testify to that, but he can elaborate on the testimony as to the services that the other witnesses have given.

Q. Is there anything you can give us with reference to this particular service beyond that which the other two witnesses have testified to?

Mr. Licking: If the Court please, there isn't any issue in the case as to the adequacy or inadequacy of the services here. The only question in issue here, as I explained beforehand, was whether this is a service club, a social club for pleasure and non-profit services. I think the services given are quite adequate. It seems to me they are more than adequate for the [103] money.

The Court: It seems to me that what has been testified to in this record should be sufficient. But if counsel wishes to go into it further I will hear it.

Mr. Licking: If counsel will say what this witness will testify to I think I can probably stipulate to it for the record.

The Court: Very well.

Mr. Deibert: I don't know that I can do that, your Honor, but I think the witness, himself, can give us the details.

The Court: I have asked the question what—I will repeat it to him: Is there anything you can add to the statements made in the testimony given by the two previous witnesses as to the road signing service of the club?

(Testimony of James W. Johnson.)

A. We have added materially to the National Uniform Code for Highway Signing, which is particularly a national problem rather than a State, which is a service to not only California, but all motorists, for one point.

Mr. Deibert: Q. What do you do—

The Court: Anything else?

Mr. Deibert: Pardon me?

The Court: Anything else?

A. Nothing in general, no.

The Court: Well, specifically, if there is anything you can add you may do so.

A. I can't think of anything— [104]

Mr. Deibert: Q. What do you do with respect to the replacement—

Mr. Licking: Remind him of something. The witness has said he does not know of anything himself. I wonder if you can remind him of anything.

Mr. Deibert: Yes, I think I can.

Mr. Licking: Go ahead and ask him.

Mr. Deibert: What, if anything, does your department do with reference to maintaining, cleaning, repairing and renewing road signs?

A. We have fourteen trucks that spend 75 per cent of their time in making repairs to signs, cleaning and repairing posts, and doing all work to improve the appearance of the sign, and all this work is done with members' dues taken from the association, without any reimbursement, at all.

Q. Just what appears on these road signs?

A. They are road signs of different types, park-

(Testimony of James W. Johnson.)

ing signs, restriction signs, signs for resorts, signs for places of historical value. We are now engaged in special historical signs for this 100-year convention or celebration that is to be held.

Q. Who bears the cost of manufacturing the road signs?

A. The California State Automobile Association.

Q. Do you also bear the cost of erecting and maintaining them? A. Yes. [105]

Q. What amount did the association spend out of its own funds and not reimbursed by State or local authorities for road signing work during the years 1943 and—'43 first.

Mr. Licking: If the Court please, this is entirely immaterial, the amount that was spent. I can't see what it has to do with the issues.

The Court: Overruled.

A. \$61,571.

Mr. Deibert: Q. In 1944. A. \$64,178.

Q. Were those normal amounts to spend for those purposes? A. No, they were not.

Q. Will you explain that?

A. The reason being that we were expanding our services for war efforts, trying to economize on labor and materials. Of course, labor and materials were difficult to get and we were also trying to avoid the erection of any signs that were not absolutely essential. Most of our work during those two years was confined to war work rather than to the general directing of traffic.

(Testimony of James W. Johnson.)

Q. Did you do any material road signing in war work?

A. Yes, we handled all of the dim-out work, involving some 8000 dim-out signs for the Army. Of course, there was a lot of damp work—

Mr. Licking: If the Court please, this is a patriotic gesture, but I can't see what materiality it has to the case. [106]

The Court: It has some bearing on the non-profit feature.

Mr. Licking: Well, if the Court please, the figures are there. This is simply an explanation of an item that is already there. I can't see what bearing it has on profit. There isn't any contention that this was something new that just occurred to them. These deductions are taken for that. These income tax returns are filed. It is in there.

The Court: Overruled.

Mr. Deibert: Q. Are you familiar with the joint committee on uniform traffic control devices?

A. Yes, I am.

Q. Describe the organization of that committee.

Mr. Licking: What materiality has that?

Mr. Deibert: It is another function of the Association.

Mr. Licking: Ask the question.

Mr. Deibert: This gentleman is very familiar with it.

Mr. Licking: That is another activity?

Mr. Deibert: That is another activity, yes.

Mr. Licking: All right, I will stipulate to it.

The Court: I will allow it.

(Testimony of James W. Johnson.)

The Witness: A. It is an organization composed of representatives of the American Association of State Highway Leaders and a member from the Association of Traffic Management, and a member from the National Conference of Street and Highway Safety, and it is headed by the Deputy Director [107] of the Bureau of Public Roads at Washington.

Q. Are you a member? A. Yes, I am.

Q. What functions does the committee perform?

Mr. Licking: Again, if the Court please, I renew the objection. This is entirely irrelevant.

The Court: Well, whatever the plaintiff in this case does would be relevant.

Mr. Deibert: This is an activity of the Association, your Honor, of the plaintiff acting through this witness here, which is carried on at the expense of the Association.

The Court: Q. Well, what is done by you as the Engineer of the California State Automobile Association in that respect?

The Witness: A. I attend different meetings regularly in Washington, where we design standard uniform traffic control devices.

Mr. Licking: I take it the question to ask is—the question is, who pays for that. Is it paid for by the Association?

A. Yes, they pay my entire expenses involved in this work.

Mr. Deibert: Who pays for the drafting and preparation of maps distributed to members of your Association?

(Testimony of James W. Johnson.)

A. California State Automobile Association.

Q. Have you any part in it? [108]

A. Yes, I have charge of that work.

Q. How many people are employed in that work? A. We have five full-time draftsmen.

Q. Are they constantly making and revising maps? A. Yes, they are.

Q. Who pays the expense of such work?

A. California State Automobile Association.

Mr. Deibert: Take the witness.

Mr. Licking: I have no questions.

The Court: That is all.

Mr. Deibert: Mr. Duke.

CECIL H. A. DUKE,

called as a witness on behalf of the plaintiff; and being first duly sworn, testified as follows:

Direct Examination

Mr. Deibert: Q. Where do you reside?

A. 1120 Union Street, San Francisco.

Q. By whom are you now employed?

A. The California State—

Mr. Licking: Counsel, what is intended to be proved by this witness? I probably will be able to stipulate to it.

Mr. Deibert: No, I don't think you can, I am sorry, but we expect to get some details in here that I can't remember myself that I think have a very direct bearing on the very [109] issue in this case, your Honor.

Q. In what capacity are you employed?

(Testimony of Cecil H. A. Duke.)

A. Assistant Manager of the Touring Bureau.

Q. At what address?

A. 150 Van Ness Avenue.

Q. How long have you been employed by the Association?

A. Sixteen years.

Q. How long have you occupied your present position?

A. Sixteen years, sir.

Q. What are your duties?

A. My particular duty is to oversee the entire function of the Touring Bureau, to see that the activity is carried out properly. My particular crew has the responsibility of attending to all of the wants—issuance of maps to our members who are going on their vacation trips throughout the year.

Q. What maps does the Touring Bureau distribute to your membership?

A. A very great number, your Honor, of maps of the western part of the United States.

Mr. Licking: Well, if the Court please, it seems to me the fact of the services is material; the extent is immaterial. They furnished such services; there is no argument about that.

The Court: Overruled. [110]

The Witness: A. Very, very extensive, your Honor. United States maps, maps of the western United States, maps of individual states, maps of the various parks that we have in the West, maps of the new Alcan Highway to Alaska, maps of the Pan-American Highway, and so on. In addition to sectional maps we have strip maps and strip-tease maps.

(Testimony of Cecil H. A. Duke.)

Mr. Licking: Strip-tease?

Mr. Deibert: Q. Does your Bureau distribute to your membership lists of hotels, lodgings, restaurants, and so forth?

A. We do. Not only a list of hotels and motor lodges in the western United States, but also an additional list covering the whole United States giving the accommodations that are available throughout this country and Canada.

Q. Does the Touring Bureau have available for members any other information?

A. Yes, a very large source of information which we have compiled over a number of years.

For your Honor's information, in the course of a man's inquiry regarding his vacation trip, there is a great deal of information that he must have and which the average person does not have. He wants to know where he will stay, what roads he is to go over, what conditions he will encounter on the road, what facilities are available for camping, what the fishing conditions are in the immediate area in which he [111] plans to travel, what restrictive seasons are imposed insofar as open and closed seasons, and so on. That information is all vitally important to him and he cannot know it beforehand unless he himself has spent in the immediate area a considerable amount of time.

Q. Does the Touring Bureau supply any publications to keep the members informed of road conditions throughout the state?

A. Yes. Not only do we have a daily bulletin which gives a recap of the pertinent information

(Testimony of Cecil H. A. Duke.)

concerning the entire west, but we also have bulletins covering the entire United States, and for that matter, Canada, and furthermore, particularly during the winter months when it is all imperative to know about particular conditions on a particular road, we resort to telephone or telegraph to acquire that information and file it so it will be available when a member asks for that information.

Q. What, if anything, does the Touring Bureau do with respect to rendering automobile registration service?

A. We do that. That again is a very, very great convenience to the members.

If your Honor has any knowledge of the tremendously long lines that line up outside the Department of Motor Vehicles during the renewal period, you can appreciate that our members certainly gain comfort from the fact that they can come into our office and without waiting in line have their [112] license plates issued to them. Furthermore, in addition to merely issuing of a new license plate in any particular year, motor vehicle transactions oftentimes become very, very complicated. We act as a buffer in aiding the member to unravel those. I might add that sometimes the unraveling takes a considerable number of days and even months. That service is rendered the members and almost, I can say, more efficiently than the Department of Motor Vehicles can do it.

Q. Do you have any publications detailing the changes in road conditions throughout the United States?

(Testimony of Cecil H. A. Duke.)

A. Yes, we do. Again we have a daily bulletin, we have a monthly bulletin, and during periods of severe weather we have telegraphic bulletins available to all our members.

Q. Is there any other information you issue to members that you have not enumerated?

A. Yes. Most of our vacationists, or shall I say, a good percentage of our vacationists want to go hunting or fishing. We take it upon ourselves to acquire through our district officers and affiliate clubs accurate and uptodate information of local conditions, particularly in this last season, when it has been most important even to old-time fishermen to know what closures are in effect so they won't be undesignedly fishing in a stream that is closed. We have digest rulings from all the departments involved, and we keep them on file and accurately distribute to the members such information. [113]

Q. Does the Association make any charge for giving out this information to the members?

A. None whatsoever.

Q. Are you able to state the average annual number of calls, both personal and by telephone, answered by your Touring Bureau during the last five years?

A. Will you please state that again?

Q. Are you able to state the average annual number of inquiries, both personal and by telephone, answered by your Touring Bureau during the last five years?

A. Your Honor, if I can consider a second I

(Testimony of Cecil H. A. Duke.)

can give you a pretty close figure. I would say, and I believe I am being conservative in saying so, that we must handle a minimum of a half-million inquiries a year.

Mr. Deibert: Take the witness.

Cross Examination

Mr. Licking: Q. Is this definite information you have as experts along those lines?

A. We consider ourselves, shall we say, not experts, but qualified, sir.

Q. Who is the man that handles your fishing end of it? A. I beg your pardon?

Q. Who is the man that is your fishing expert?

A. A man by the name of Joe Kelstrom, sir.

The Court: You have your vacation in mind?

Mr. Licking: I haven't any further questions.

Mr. Deibert: That is all.

Mr. Licking: That is the only important question I can think of.

Mr. Deibert: Mr. E. S. Moore.

EDWIN S. MOORE,

called as a witness on behalf of the plaintiff; and being first duly sworn, testified as follows:

Direct Examination

Mr. Deibert: Q. Where do you reside?

A. 334 Bixby Street, San Francisco.

Q. By whom are you now employed?

A. California State Automobile Association.

Mr. Licking: Mr. Deibert, again I will make

(Testimony of Edwin S. Moore.)

my same request, I just want to know if this is more of the same thing.

Mr. Deibert: No. No, this is on a different line.

Q. In what capacity?

The Court: I thought you were going to offer to stipulate.

Mr. Licking: I was.

The Court: If Counsel will state what he intends to bring out by this witness—

Mr. Licking: I probably would, but he said it was a [115] different deal.

Mr. Deibert: It isn't too long, your Honor, but it is one of the important activities of the Association.

The Court: I thought you might state to Counsel what you expected to prove by this witness.

Mr. Licking: I probably will be able to stipulate to it.

Mr. Deibert: This witness, I think, when he answers my question will indicate what his line of activities is very briefly.

The Court: Very well.

Mr. Deibert: Will you answer the question?

(Question read.)

A. I am Manager of the Public Relations Department of the California Automobile Association, which includes the activities of the Association, including its public safety work, its highway activities, and its legislative activities.

Q. What is your business address?

A. 150 Van Ness Avenue, San Francisco.

Q. How long has you been employed by the

(Testimony of Edwin S. Moore.)

Plaintiff? A. Now in my 21st year.

Q. How long in your present position?

A. Since 1932—not the present department—I would correct that—as assistant to the head of that department, but head of that department for the past five years.

Q. Who directs the Public Safety Department for the Association? [116]

Mr. Licking: If the Court please, what is the materiality of who directs the Public Safety Department?

Mr. Deibert: It is a part of the picture of the work that is done and a very important work.

The Court: He may answer.

The Witness: A. The Public Safety activities of the Association, of the Automobile Club, come directly under the Public Safety Committee of the Board of Directors. I am in charge of carrying out the activities themselves as an employee of the California Automobile Association.

Mr. Deibert: Q. What was the purpose of establishing your Public Safety Department?

A. The Public Safety Department of the Automobile Club was organized to carry out one of the functions—

Mr. Licking: It has something to do with public safety, I take it. I will stipulate to it.

Mr. Deibert: It has to do with public safety, but I would like the witness to answer, if I may, your Honor.

The Court: Yes.

(Testimony of Edwin S. Moore.)

Mr. Licking: After all, the witness can't testify as to the purpose, if the Court please.

The Court: Well, tell us what you do in that regard?

The Witness: A. The Automobile Club conducts many safety activities. Starting with the grade school levels, the Association sponsors and develops and presents materials for [117] safety educational work, starting at the kindergarten level and through the various grades of the elementary schools, and into the high schools and college levels.

Q. What safety services does the Association render to the elementary schools?

A. Starting with the elementary schools and beginning with the kindergarten classes, the Automobile Association prepares and distributes crayon lessons for the very young children in traffic safety and kindred problems of safety, and with the grade schools, that is, from the first grade up through the eighth, safety posters and safety lessons are distributed.

Q. How many safety posters and lessons were distributed through 1943 and 1944 to the elementary schools in California and Nevada, which is your territory?

A. In 1943 and 1944, due to the war situation the number of safety posters and lessons distributed by the Automobile Club were cut in half. During those two years we distributed instead of eight issues each school term, we distributed four issues

(Testimony of Edwin S. Moore.)

each school term, consisting of 15,000 safety posters each month and a corresponding number of safety lessons.

Q. That was each month?

A. They were distributed in sufficient quantity—there were only four issues in each of those two years, instead of the customary eight. [118]

Q. What did these safety posters and lessons contain?

A. The safety posters depict some particular traffic hazard which we feel is desirable to emphasize, and the lessons which accompany the posters demonstrate the proper and correct way of meeting that particular hazard and condition. The posters and lessons are designed for use by the pupils and the teachers of the grade schools to enable them to better understand the problems involved in traffic safety and to meet the daily traffic situations as they occur.

Q. What is the reaction of teachers and principals to this work?

Mr. Licking: Well, if the Court please, this is purely irrelevant.

The Court: I think so. Sustained.

Mr. Deibert: I beg your pardon? I didn't hear that.

Mr. Licking: I objected on the ground it was irrelevant, and he sustained the objection.

Mr. Deibert: I see.

Q. Have you knowledge of the results of this program?

(Testimony of Edwin S. Moore.)

Mr. Licking: Same objection, if the Court please.

The Court: Sustained.

Mr. Deibert: May I say this, your Honor—I, of course, respect your ruling, but it seems to me we ought to be able to develop here whether or not this activity of the Association is a worthwhile activity, whether it is doing anything [119] for the communities in safety—

The Court: Oh, it is axiomatic it is worth while. I don't see any occasion to develop that further.

Mr. Licking: I will stipulate — if the Court please, I am perfectly willing to stipulate that a safety program is a worthwhile activity.

Mr. Deibert: Q. Does the Association participate in the operation of school safety patrols?

A. Yes. The Association sponsored and developed the idea of school safety patrols as far back as 1923, when the first safety patrol was organized in San Francisco.

Q. What is the function of the school safety patrols?

A. The school safety patrols' sole purpose—the main purpose, at least, of the school safety patrol is to take certain of the more responsible students in a school and train them to guard and protect their classmates at street crossings in and about the neighborhood of the schools, thereby instructing younger children in the safe and proper way of crossing streets and the proper locations or proper crossings to use.

(Testimony of Edwin S. Moore.)

Q. What materials are furnished school safety patrols?

A. The Automobile Club furnishes white Sam Browne belts, identification cards, special certificates of award at the close of the term which the young patrol members are serving, and also certain awards for the schools themselves where the [120] boys have been most efficient in their operation.

Q. Is there any charge made for the safety posters and lessons or other materials you have mentioned?

A. The Association furnishes all these materials I have mentioned without any charge.

Q. What activities does the Association carry on in high schools and colleges?

A. Again, the Association has been instrumental in sponsoring a program for driver education in high schools and colleges in California.

Q. What materials are used in this program?

A. The Automobile Club has developed a course for high school use called "The Driver of Tomorrow", that is published by the club and furnished free of charge to the high schools in our territory.

In addition the American Automobile publication known as "Sportsmanlike Driving", which is probably the most comprehensive and complete textbook on the subject of driver training in the United States and widely used throughout the United States, is also distributed by us.

Q. How many high schools in California have courses in driver education?

(Testimony of Edwin S. Moore.)

Mr. Licking: If the Court please, this is getting too far afield.

The Court: Overruled. [121]

The Witness: A. In the past year a survey indicated that over three hundred high schools in California here had held classes in either driver education or driver training, or both phases of that subject.

Mr. Deibert: Q. Does the Association conduct any traffic surveys?

A. Yes. The Association also has a traffic survey service.

Q. What is the nature of that service?

A. A traffic survey service is a service which is available to cities, communities and organizations where the organization or the community itself does not have sufficient funds to employ its own traffic engineers, but they do have traffic problems of one type or another, usually involving or affecting the handling of traffic in the community or the safety of traffic in the community, and in this connection the Automobile Club will undertake a traffic survey at its own expense for the community and develop plans and recommendations to meet their problems and in turn assist the community in putting those recommendations into effect.

Q. Do you make any charge for this service?

A. There is no charge for this service.

Q. Have you participated personally in any attempts to obtain legislation from the state legislature affecting motorists?

(Testimony of Edwin S. Moore.)

A. Yes. Among my other duties I happen to be legislative [122] representative of the Association.

Q. Has that been carried on to any great extent in the past few years?

A. Yes. The Automobile Club has been very active through the years and at the present time in the development of adequate and sound motor vehicle legislation and also in the development of sound and adequate highway improvement programs. The record will show, and I know personally since the time I have been in the Automobile Association, because I have participated in many of those programs myself, that we have been most active in developing the highway programs which have meant so much in the development of our highway system in California.

Q. Have you done anything of a similar nature with respect to local ordinances?

A. Yes. Again the Automobile Association has undertaken to promote a uniform traffic code for all cities so that motorists travelling—our members and others travelling from one community to another might meet with the same general local traffic regulations in whatever community they might be.

Q. Did your Association in 1943 and 1944 have any connection with a National Pedestrian Protection contest?

A. Yes. We sponsored that contest in California in both of those years. [123]

Q. What did you do in that connection?

A. We enrolled cities throughout the State in

(Testimony of Edwin S. Moore.)

the Pedestrian Protection contest, also the State of California. Of course, the purpose being to again bring to the attention of the authorities and to the public, as well as our members, the problem involved in the pedestrian hazard.

Our studies demonstrated that in the larger cities approximately three out of four traffic fatalities involved pedestrians, and in the smaller cities approximately fifty per cent of fatalities involved pedestrians.

Mr. Licking: If the witness is reading from a report, I have no objection to putting the report in.

The Witness: A. I am not reading from anything.

Mr. Deibert: He is not reading anything.

A. No, I have here a number of files I brought with me showing the materials—

Mr. Licking: I was just thinking if you had some report it could go in. I haven't any objection to its being deemed read into evidence.

The Witness: A. I was addressing myself to the Pedestrian Protection contest and the activities which the Association engaged in in connection with the particular program designed to help provide greater protection to pedestrians, because, as I indicated, our members are both pedestrians and drivers on occasion, and since the pedestrian hazard is a most serious [124] one, we felt it was a worth while activity to provide as much aid physically as could be offered and to do as much educational work as we could do in that field.

(Testimony of Edwin S. Moore.)

Q. Does your Association do any of that work by radio?

A. Yes. We have a series of weekly radio programs on safety work.

Q. Will you describe in a little more detail what you do in that connection?

A. In the years 1943 and 1944—I will address myself to those particular years—we had three regular weekly fifteen minute safety radio programs over radio stations in our territory, which is northern and central California. Those programs were presented as public service programs in the interest of public safety jointly by the radio stations participating and the Automobile Club, the radio station donating its time and facilities and the club preparing material for broadcasting purposes and presenting the programs in that particular field.

Q. Does your Association do anything with respect to films in connection with safety work?

A. Yes. We maintain a film library, a safety film library, and distribute safety films to teachers, schools, clubs and groups interested in traffic safety and the problems involved on the streets and highways, and ways and means of overcoming those problems. [125]

Q. How many films do you have in the library, do you know?

Mr. Licking: It seems to me how many films is not relevant.

The Court: Overruled.

The Witness: A. I might refer to a list which I brought with me, because I don't know if I can

(Testimony of Edwin S. Moore.)

recollect offhand, but we do have, I would say, about—well, I can give you it precisely. There are 23 films on our film list which we maintain.

Mr. Deibert: Q. And are they distributed for use throughout your territory?

A. Yes, they are available without charge to any organization, group, school or college, or any individual who would like to have a film on traffic safety.

Q. Does the Association engage in other safety programs in addition to those you have already described?

A. We do. The Automobile Club has since 1938 each year, and that would include the years 1943 and 1944, sponsored summer session coaches at the University of California in driver education and driver training, both for high-school teachers and for the benefit of fleet operators and others interested in learning the problems in modern traffic and ways of selecting and training drivers and the ways and means of avoiding accidents, developing sound driving practices. This of course, as I say, was given in 1943 and 1944, [126] as well as subsequent years and prior years.

Q. Are there any other safety activities in which you engage which you have not mentioned?

A. Without having a list to go over, I don't recollect right now if we have other activities.

Mr. Deibert: Take the witness.

Mr. Licking: No questions.

The Court: That is all.

Mr. Deibert: Mr. Addison G. Strong.

ADDISON G. STRONG,

called as a witness on behalf of the plaintiff: and being first duly sworn, testified as follows:

Mr. Deibert: Your Honor, I might say for your information Mr. Strong is a member of the certified public accounting firm of Hood and Strong of this city, and has been the auditor and accountant for plaintiff in this case over a long period of years, and I thought perhaps if we could stipulate to that fact we might save time and a good deal of effort to qualify him.

Mr. Licking: I will stipulate that he is qualified—

The Court: Why don't you broaden the stipulation and suggest to Counsel what you expect to prove by him?

Mr. Licking: I will further stipulate that Mr. Strong prepared or supervised the preparation of the figures which [127] were submitted with Mr. Watkins' affidavit and those figures that appear in the income tax returns which are already on file.

Mr. Deibert: Yes.

Q. That is correct, isn't it? A. Yes.

The Court: Is that what you want to prove?

Mr. Deibert: No, that is not the purpose, your Honor.

Mr. Licking: What is it?

Mr. Deibert: The purpose is to show whether there were any deficiencies or net incomes at the end of the various years going back—we have not gone back to the inception of the Association, but

(Testimony of Addison G. Strong.)

we have taken the years from 1931 to 1941, inclusive.

The Court: Isn't that in evidence?

Mr. Deibert: No.

Mr. Licking: Counsel, that is already in evidence.

Mr. Deibert: No, I beg your pardon, they are not in evidence—are they, Mr. Strong?

A. No, not in entirety.

Mr. Licking: They are here. It shows some years there was a loss and some years a profit.

The Court: Yes, there was an exhibit that showed that.

Mr. Licking: Yes, from 1931 to 1940, showing profit and loss. It is a part of Exhibit 1, part of Watkins' affidavit. [128]

Mr. Deibert: What I hold in my hand, your Honor, is a statement made by Mr. Strong showing the position of the surplus balance, and that is, in its entirety, in the exhibit which is attached to Mr. Watkins' affidavit.

Mr. Licking: Very well, the books will be the best evidence. If the books are not here I can't cross-examine the witness.

Mr. Deibert: Well, these figures have been taken— How did you get these figures?

A. I got them from the books.

Q. Directly from the books?

Mr. Licking: Well, if the books are not here. I can't cross-examine the witness and I object to the compilation.

(Testimony of Addison G. Strong.)

The Court: That is true, he can't cross-examine the witness if the books are not here, if he is testifying from a recap of the books.

Mr. Deibert: May he not testify from a compilation, your Honor, which he took directly from the books?

The Court: Well, the difficulty is that Counsel cannot cross-examine him without the books being present.

Mr. Deibert: I think he can cross-examine him from this statement which is a resume of the books.

Mr. Licking: (referring to document): What are the doughnuts on here supposed to represent?

Mr. Deibert: The figures in red, and those are the [129] deficiencies.

Mr. Licking: Those are the deficiencies?

Mr. Deibert: Yes, those are the deficiencies.

Mr. Licking: All right, I will stipulate it can be introduced in evidence as your exhibit without any examination.

Mr. Deibert: Very well.

The Court: For what years does it cover?

Mr. Licking: It covers the years apparently from 1931 through 1947.

Mr. Deibert: No, for the first quarter of 1947.

Mr. Licking: For the first quarter of 1947. It shows certain years where there is an excess of income over current expenses. There is one thing, your Honor, the bookkeeping system and the returns of the organization are on a cash basis.

Mr. Deibert: That is right.

(Testimony of Addison G. Strong.)

Mr. Licking: They don't show accruals.

Mr. Deibert: No.

Mr. Licking: And in that connection I will state frankly that some of the years they took in more than they spent and in some of the years they did not, and in these particular years they took in more than they spent, and that is the reason the tax was assessed.

The Court: "In these particular years," you mean 1942 [130] and 1943?

Mr. Deibert: Well, it covers the entire period.

Mr. Licking: 1944 and 1945.

The Court: When you say in these particular years there was a net profit—

Mr. Deibert: Yes, there was for those two years, but this statement shows the trend beginning in 1934.

Mr. Licking: Well, what the trend is is a matter of argument.

The Court: Well, you stipulate it may come into evidence. If you offer it I will receive it.

Mr. Deibert: I will offer it.

The Court: Offered and received.

Mr. Licking: May I make these in red? (circling figures in red pencil.)

(The document in question was thereupon received in evidence and marked Plaintiff's Exhibit 4.)

Mr. Licking: Have you copies of this?

Mr. Deibert: No. May I have this copy for the purpose of making copies, your Honor?

(Testimony of Addison G. Strong.)

Mr. Licking: I will stipulate it may be withdrawn in order that copies may be photostated or otherwise made.

The Court: Very well.

Mr. Deibert: Thank you, and I will furnish you with copies, Mr. Licking. That is all, Mr. Strong.

The Court: Any cross-examination?

Mr. Licking: None, your Honor. The figures speak for themselves.

Mr. Deibert: That concludes our case, your Honor.

Mr. Licking: If the Court please, for the Court's convenience I will offer in evidence now G.C.M., General Counsel's Memorandum No. 23,688, which was the basis of the assessment in the case.

Mr. Deibert: That is contained in an official publication of the Government, your Honor, but we have no objection.

Mr. Licking: It is just for the convenience of the Court.

The Court: Very well.

Mr. Licking: Those special publications, I happen to know, are not available in the library at Sacramento.

(The document in question was thereupon received in evidence and marked Defendant's Exhibit C.)

Mr. Licking: I had that in mind. The Government will rest its case.

The Court: I understand that both sides rest?

Mr. Deibert: Yes, your Honor.

Plaintiff rests.

Defendant rests.

The Court: What is the pleasure of Counsel? Did you wish to have this submitted on briefs? [132]

Mr. Deibert: I would prefer to do that, your Honor. There are a great many facts in the case, there are some questions of law, and we think it might properly be submitted on briefs.

(Discussion as to filing briefs.)

The Court: 45, 45 and 20, and the 20 to start after the brief is delivered to you, and upon filing that closing brief it will stand submitted.

CERTIFICATE OF REPORTER

I, Clarence F. Wight, Official Reporter, certify that the foregoing 132 pages is a true and correct transcript of the matter therein contained as reported by me and thereafter reduced to typewriting to the best of my ability.

/s/ CLARENCE F. WIGHT.

[Endorsed]: Filed March 2, 1948.

[132-a]

[Endorsed]: No. 12055. United States Court of Appeals for the Ninth Circuit. James G. Smyth, Collector of Internal Revenue of the First Internal Revenue Collection District of California, Appellant, vs. California State Automobile Association, a corporation, Appellee. Transcript of Record. Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed October 1, 1948.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 12055

JAMES G. SMYTH, Collector of Internal Revenue
of the First Internal Revenue Collection District
of California,

Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,

Appellee.

APPELLANT'S STATEMENT OF POINTS IN-
TENDED TO BE RELIED ON ON APPEAL
AND DESIGNATION OF PORTION OF
RECORD TO BE PRINTED

Appellant adopts as points on appeal the state-
ment of points filed with the court below and in-
cluded in the Transcript of Record on file herein.

Appellant designates for printing the entire
Transcript of Record on file herein except that, as
to the Exhibits in evidence the same may be consid-
ered by the Court in their original form.

/s/ FRANK J. HENNESSY,
United States Attorney.

/s/ WILLIAM E. LICKING,
Assistant U. S. Attorney,
Attorneys for Appellant.

ORDER

Ordered exhibits may be so considered.

WILLIAM DENMAN,
Chief Judge, U. S. Court of Appeals for the Ninth
Circuit.

[Endorsed]: Filed November 4, 1948. Paul P.
O'Brien, Clerk.

No. 12,055

IN THE

United States Court of Appeals
For the Ninth Circuit

JAMES G. SMYTH, Collector of Internal
Revenue of the First Internal Revenue
Collection District of California,
Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,
Appellee.

On Appeal from the United States District Court for the
Northern District of California.

BRIEF FOR APPELLANT.

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FILED

DEC 28 1948

PAUL P. O'BRIEN,

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No. 12,055

IN THE

**United States Court of Appeals
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JAMES G. SMYTH, Collector of Internal
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Collection District of California,
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vs.

CALIFORNIA STATE AUTOMOBILE ASSO-
CIATION, a corporation,
Appellee.

On Appeal from the United States District Court for the
Northern District of California.

BRIEF FOR APPELLANT.

OPINION BELOW.

The opinion of the District Court (R. 67-78) is reported in 77 F. Supp. 131.

JURISDICTION.

This appeal involves Federal income and excess profits taxes for the calendar years 1943 and 1944. (R. 4.) The taxes in dispute are in the amount of \$232,865.12 and were paid on September 15, 1945. (R. 81.) Claims for refund were filed on October 23,

1945. (R. 81.) More than six months after the filing of the claims and within the time provided in Section 3772 of the Internal Revenue Code or on May 26, 1948, the taxpayer brought an action in the District Court for recovery of the taxes paid. (R. 2-63.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1340. The judgment was entered on March 24, 1948. (R. 90-91.) Within sixty days and on May 20, 1948, a notice of appeal was filed (R. 91-92) pursuant to the provisions of 28 U.S.C., Section 1291.

QUESTION PRESENTED.

Was taxpayer, during the taxable years 1943 and 1944, a club, organized and operated exclusively for pleasure, recreation and other nonprofitable purposes within the meaning of Section 101 (9) of the Internal Revenue Code?

STATUTE INVOLVED.

Internal Revenue Code:

Sec. 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

The following organizations shall be exempt from taxation under this chapter—

* * * * *

(9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder;

* * * * *

[26 U.S.C. 1946 ed., Sec. 101.]

STATEMENT.

The District Court found the facts substantially as follows (R. 80-86):

Taxpayer was organized under the laws of California in 1907 as a nonprofit corporation, the purposes of which are substantially as follows (R. 82):

(1) To promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users.

(2) To urge adoption of just and intelligent legislation on the use of highways and the regulation of traffic thereon.

(3) To maintain offices for collecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles.

(4) To protect the legitimate interests of its members in connection with its purposes.

(5) To affiliate and associate with similar organizations.

The District Court also found (R. 83-84) that taxpayer, in furtherance of its purposes, "provided" during 1943 and 1944 the following:

(1) A Touring Bureau which provides the members with complete touring data and assists them in planning motor trips.

(2) An Emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter

automobile trouble on the highways, which service is restricted to passenger cars.

(3) A Road Sign Department, which operates in conjunction with state and local authorities, a service consisting of the erection and maintenance of direction and warning signs and historical markers.

(4) A Public Safety Department, which carries on an active and aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions.

(5) An Adjustment and Traffic Department, which advises and assists the members with respect to traffic violations and accidents.

(6) A License Department, which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtaining automobile license plates, as well as Federal auto tax stamps.

(7) A Magazine Department which publishes and distributes free to the members a magazine, keeping them informed of motoring conditions and improvements, and specializing in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no paid advertising material since January 1, 1942.

The District Court concluded (R. 87) that the “association is and was at all times here pertinent a

club within the meaning of Section 101 (9) of the Internal Revenue Code" and that taxpayer (R. 89) "was organized and operated exclusively for pleasure, recreation and other nonprofitable purposes during the years 1943 and 1944".

Judgment was accordingly rendered in favor of taxpayer in the amount of \$232,865.12, with interest (R. 90-91), representing Federal income and excess profits taxes paid for the taxable years 1943 and 1944.

STATEMENT OF POINTS TO BE URGED.

The principal point (R. 96-97) upon which the Government intends to rely is that the District Court erred in holding that taxpayer was, during the years 1943 and 1944, a club organized and operated exclusively for pleasure, recreation and other nonprofitable purposes within the meaning of the exempting statute.

SUMMARY OF ARGUMENT.

Taxpayer was not a club within the meaning of Section 101 (9) of the Internal Revenue Code, since it had none of the attributes commonly associated with a club. That is, there was no provision made for social intercourse, its membership was unlimited, new members were not selected by ballot or otherwise chosen by members of the association, and there was no group activity or other club functions. It was merely an association organized and operated to render service to its

members in the operation of their automobiles and to promote and encourage highway construction and safe driving.

The taxpayer did not come within the statute for the further reason that it was not organized nor was it operated in 1943 or 1944 exclusively for the pleasure or recreation of its members. The undisputed facts clearly show that little, if any, of its activities were devoted to such purposes. The principal services rendered by taxpayer to its members consists primarily of insurance, road service and travel advice. Its other activities were of a semi-public nature having to do with highway construction and assisting state and local authorities in connection with traffic signs.

It is the Government's position that such activities were not sufficient to establish that taxpayer was organized and operated *exclusively* for the purposes specified in the exempting statute.

ARGUMENT.

TAXPAYER WAS NOT A "CLUB" UNDER THE ACT NOR WAS IT ORGANIZED AND OPERATED EXCLUSIVELY FOR PLEASURE OR RECREATION.

Section 101 (9) of the Internal Revenue Code, *supra*, exempts from Federal income taxes certain types of "associations", including "Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes". Taxpayer contends that it comes within the exemption. The Government takes the position that, on the undisputed facts, taxpayer

cannot bring itself within the exempting statute because (1) taxpayer is not a "club" within the meaning of the Act and (2) taxpayer was not "organized and operated *exclusively* for pleasure, recreation, and other [similar] nonprofitable purposes". (Italics supplied.)

That taxpayer is not a club for the purposes here concerned, seems clear. In the absence of a statutory definition or helpful legislative history it seems appropriate to conclude that Congress intended by the section to exempt organizations which are usually and commonly referred to as clubs. The word "club" is defined in Webster's New International Dictionary (Second ed., 1948), p. 509, as follows:

6. An association of persons for the promotion of some common object, as literature, science, politics, good-fellowship, etc., esp. one jointly supported and meeting periodically. Membership is usually conferred by ballot, and carries the privilege of exclusive use of club quarters.

A similar definition is found in Funk & Wagnalls' New Standard Dictionary (1947 ed.), p. 506, as follows:

An organization of persons who meet for social intercourse or other common object, the members of which are usually limited in number and chosen by ballot; * * *

Taxpayer's members do not, as such, meet for social intercourse (R. 133) nor is its membership limited in number. (R. 136.) Moreover, membership is not conferred by ballot and members have no means of pass-

ing on the admission of new members. (R. 137.) In addition, taxpayer has no clubhouse or other meeting place. We find little, if anything, about taxpayer which makes it a club within the definitions of the word.

The Court below concluded that (R. 87) "A club is an association the expenses of which are shared among its members" and also concluded that (R. 87):

To constitute a club within the meaning of Section 101 (9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity.

We find no support for the conclusion that the mere sharing of expenses among individuals gives to the group the aspect of a club. Certainly that would not suffice as a definition of sufficient persuasion to import Congressional intent that no more would be needed to qualify under the statute. While it is true that the use of the word "club" does not necessarily carry with it the idea of social intercourse, it usually does so. It is incumbent upon taxpayer before it can enjoy the privileges of an exempting statute to show that it comes within the Act. It is not sufficient that taxpayer show that it is not necessarily excluded from the benefits, it must make a clear showing in the affirmative. It is common knowledge that when we refer to a club, we think of a clubhouse or some other place where the club members may meet socially. That is clear from the dictionary definitions.

It is difficult to understand what the lower Court had in mind by saying that "it is sufficient if its members make a common cause in a financial * * * sense". (R. 87.) If the Court had in mind that a "club" within the meaning of the Act could be no more than a group of people interested in saving money on insurance and automobile service charges, we see no support whatever for the conclusion. It may be that the Court had in mind the exemption of business leagues, crop financing operations, domestic building and loan associations, fruit growers' associations, holding companies, teachers' retirement fund associations or the like. If so, they are covered by other subdivisions of Section 101 of the Internal Revenue Code and have no place in construing subsection (9), devoted exclusively to "clubs".

The entire record clearly shows that taxpayer has no activities commonly associated with club functions. Almost any motorist is familiar with so-called automobile clubs of which taxpayer is a typical example and it is common knowledge among motorists that such organizations are attractive solely because of the service they render the members in the operation of their automobiles and the insurance advantages afforded. It is sheer nonsense to suggest that anyone joins any so-called automobile club for any other reason than to receive the benefits offered in that direction. If he thinks about joining an association of this kind, his first and only consideration is whether or not the services and reduced insurance rates are worth the dues he will be required to pay. In no case

does he consider that he is joining the so-called "club" for pleasure or recreation.

It is significant also, in determining what Congress meant by "clubs", to note that Congress had in mind "pleasure" and "recreation". The indication is that the word "club" was used in the ordinary sense. Published administrative interpretation is to that effect. In G.C.M. 23688, 1943 Cum. Bull. 283, 286-287, the question is discussed as follows:

Although there is no statutory definition of the term "club," as used in section 101 (9) of the Code, it is believed that the term contemplates a commingling of members, one with the other, in fellowship. Thus, an organization should be so composed and its activities be such that fellowship among the members plays a material part in the life of the organization in order for it to come within the meaning of the term "club." * * *

The term "clubs," as used in section 101 (9) of the Code, *supra*, is used in the same sense as the term "club" is used in section 1710 of the Code and corresponding sections of the Revenue Acts relating to the taxation of dues or membership fees paid to "any social, athletic, or sporting club or organization." (See G.C.M. 13067, *supra*.)

In *Arner v. Rogan* (May 20, 1940, unreported), the District Court of the United States for the Southern District of California, Central Division, had occasion to consider whether the Biltmore Health Club was a "club" within the meaning of section 501 of the Revenue Act of 1926, as amended by section 413 (a) of the Revenue Act of 1928 (now section 1710 of the Code). In conclud-

ing that the organization was not a club, the Court said:

* * * at least there must be some sort of association or cooperation between the members in an effort to reach some common objective before we may consider that there is a club or organization.

In the course of its opinion, the Court observed:

The evidence shows that members never met together or in committee and never participated in any activities which are normally carried on by members of clubs or similar organizations, nor is there evidence that the patrons were entitled by the terms of their contracts to so participate. * * *

Another factor given weight by the Court was that:

* * * the Biltmore Health Club did not in practice restrict its membership, nor did it agree to do so. The only qualifications apparently were that the applicant be over 21, white, free from any contagious disease or dangerous physical condition, and able to pay the fees.

The necessary implication to be derived from the *Arner* case is that financial contribution by way of a fee charged by the organization does not amount to "association or cooperation between the members in an effort to reach some common objective," but that there must be some participation by the members in activities ordinarily carried on by clubs, which activities are intended to culminate in the realization of a common objective.

Although that ruling was issued in connection with a so-called automobile club differing in some respects from taxpayer, it will be seen that under the ruling taxpayer would not be exempt since it does not have the necessary attributes of a club and because it was not organized or operated exclusively for the purposes specified in the statute.

We think it is equally clear that taxpayer was not organized and operated exclusively for pleasure or recreation. The words of the statute "and other non-profitable purposes" do not, under the familiar rule of *ejusdem generis*, enlarge the meaning of the preceding words of the statute. Otherwise the word "exclusively" would be meaningless and the words "pleasure" and "recreation" would be mere surplusage.

There is no doubt that taxpayer does render an important public service in the promotion of good highways and safe driving. However, that fact is entirely immaterial in determining whether taxpayer is a club or whether it functions for the pleasure and recreation of its members. No doubt the members find considerable satisfaction and comfort in knowing that they will be towed to a garage (R. 130, 144) if necessity requires, or that an attorney of the association will come to their rescue in the event of arrest for a traffic violation. (R. 128.) The privilege of obtaining travel information and license plates without inconvenience (R. 160) as well as the privilege of obtaining inexpensive insurance (R. 140) is very pleasing to the members. However, that is not, we think, the pleasure

Congress had in mind in limiting the application of the exemption. Further, it cannot be seriously contended that rendering such services to its members puts the association in the category of operating "exclusively" for the promotion of pleasure and recreation. In interpreting a similar statute the Court in *Better Business Bureau v. United States*, 326 U.S. 279, held that the word "exclusive" in the statute meant just what it said and is not to be interpreted otherwise.

Taxpayer is in reality nothing more than a service organization. It renders services to its members for a consideration. The membership is large (R. 151), its net income is substantial (R. 131, Pltf. Ex. 1-H, 1-I), and its territory is extensive. (R. 149.) Anyone who has not demonstrated that he is a hazardous driver may join. (R. 136.) As above stated, there are no social aspects to the organization (R. 133) and there is nothing suggesting (except in an extremely remote way) that the recreation of its members is involved. The association will assist a member in planning a motor trip be it for a vacation or business. It does not devote all or even a substantial part of its income or of its attention to planning pleasure trips for its members.

The expression "pleasure car" might have had some factual significance when taxpayer was incorporated in 1907 but that was not so during the period here involved. Today a private car is virtually a necessity. Anyone knows that only a small fraction of the yearly

driving can be assigned to the pleasure or recreation of the driver. And so it is with the maintenance of that necessary and essential item in our daily lives. We need car service now more than ever before; however, very little of it nowadays can be assigned to pleasure or recreation expenses. Our car is needed to take us to the golf course or trout stream but pleasure and recreation starts after we get there. The golf club or rod and gun club may be income tax exempt under the section here involved, but the so-called automobile club that sends out the tow car or puts up the fine for traffic violations is a different type of organization. At least we believe most anyone, including members of Congress, would think so. To hold otherwise in applying Section 101 (9) of the Internal Revenue Code is, we submit, stretching the exempting statute to unreasonable limits. This is the first case involving an association of this kind and is quite obviously important from a revenue standpoint. We submit that the present administrative interpretation of the statute is correct and that the Commissioner of Internal Revenue was not in error in assessing and collecting the taxes here in question.

CONCLUSION.

The judgment in the lower Court should be reversed.

Dated, December 22, 1948.

Respectfully submitted,

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No. 12,055

IN THE

United States Court of Appeals
For the Ninth Circuit

JAMES G. SMYTH, Collector of Internal
Revenue of the First Internal Revenue
Collection District of California,

Appellant,

vs.

CALIFORNIA STATE AUTOMOBILE ASSOCIA-
TION (a corporation),

Appellee.

Upon Appeal from the United States District Court
for the Northern District of California.

BRIEF FOR APPELLEE.

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CALIFORNIA STATE AUTOMOBILE ASSOCIA-
TION (a corporation),

Appellee.

**Upon Appeal from the United States District Court
for the Northern District of California.**

BRIEF FOR APPELLEE.

STATEMENT.

The first paragraph under the heading "Statement" on page 3 of appellant's brief appears to be somewhat misleading in saying that "The District Court found the facts substantially as follows (R. 80-86)", inasmuch as the only facts then set forth were that appellee was organized under the laws of California in 1907 as a non-profit corporation, followed by an

enumeration of the purposes for which appellee was so organized, and the finding of the District Court that appellee provided seven enumerated services. The "Statement" then states that the District Court concluded (R. 87) that the "Association is and was at all times here pertinent a club within the meaning of Section 101(9) of the Internal Revenue Code," and (R. 89) "was organized and operated exclusively for pleasure, recreation and other non-profitable purposes during the years 1943 and 1944". The final paragraph recited that judgment was rendered in favor of taxpayer in the amount claimed, with interest, for the years 1943 and 1944.

Actually, "the facts" found by the District Court included also, among others, the following pertinent and important findings (R. 81-86):

"That Plaintiff at all times since the inception of Federal income taxation in 1913 had been exempt from the imposition of any Federal income and/or excess profits tax until it was finally advised by the Commissioner of Internal Revenue in a letter dated July 27, 1945, that further exemption was denied.

"That the purposes of the Plaintiff have been practically unchanged since its organization and at all times pertinent herein was substantially as follows: to promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users; to urge adoption of just and intelligent legislation on the use of highways and the regulation of traffic thereon; to maintain offices for col-

lecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles; to protect the legitimate interests of its members in connection with its purposes; to affiliate and associate with similar organizations. None of the foregoing or any other purposes of Plaintiff were designed or intended to make a profit.

“That the Plaintiff has only the powers necessary to carry out its purposes. The Plaintiff has no power to distribute or set aside any portion of its net income to its members or to any other person except to carry out its purposes.

“That the sum total of the activities of the Plaintiff is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by Plaintiff are for the pleasure and recreation of its members.

“That in addition to the normal activities and services of the Plaintiff during the two years here in question, Plaintiff engaged in many activities incidental to the war effort and performed many services for the general public, such as road signing as an official agency of the Federal Government in blackout and dimout areas, services in connection with gas rationing, information and advice furnished members of the armed forces, training of drivers for the Red Cross and other volunteer war services, and in arrangements of reservations and accommodations for its members.

“That none of the normal activities or the war-time activities of the Plaintiff were conducted for

the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities.

“It has been the policy of the Plaintiff to expend on services all its annual receipts, and during 1943 and 1944 it was prevented from so doing only by reason of wartime restrictions. That in the 16-year period from and including 1931 to 1946 the Plaintiff has had a deficit in 8 years and a surplus in 8 other years.

“That the Plaintiff has never distributed, set aside, or credited on its books by way of dividends or from its earnings any money to any of its members as an incident of their membership in the Plaintiff association. That there has never been any intention to distribute any net income direct to the members. That the directors of Plaintiff serve without financial remuneration.

“That the members of the Plaintiff association collectively defray all its expenses by the payment of identical membership fees and dues.

“That the Plaintiff is a continuing organization whose members make common cause both in a financial sense and in carrying out its stated purposes by group activity as well as by individual action.

“That Plaintiff has annual meetings of its members, meetings of its board of directors, and other meetings occasionally called by the Plaintiff and its standing committees, which meetings members are entitled to attend. Other than these meetings the Plaintiff has no social features. Membership is open to all owners of automobiles unless

they are considered too old, have a bad traffic record, or are otherwise irresponsible. No social, racial or religious discrimination is made with respect to membership. No memberships in Plaintiff are held by any other associations, clubs or organizations. No memberships in Plaintiff association are held by operators of trucks or commercial motor vehicles as such.

“That Plaintiff association is now and at all times pertinent hereto was certified as a ‘Motor Club’ by the State of California.

“That Plaintiff association is a club.

“That Plaintiff association is a separate and distinct organization from the California State Automobile Association Inter-Insurance Bureau. Although Plaintiff and said Bureau jointly occupy the office quarters of Plaintiff association, said Bureau compensates Plaintiff for the space the former occupies, on a square foot basis, and Plaintiff derives no profit or earnings from its relationship with said Bureau.”

It is also pertinent to note that in describing appellee’s Magazine Department under (7) on page 4 of his brief, appellant omitted the following from the trial Court’s finding: “‘There is no sale or public distribution of said magazine’”.

The conclusions of law adopted by the District Court follow (R. 87-89) :

“A club is an association the expenses of which are shared among its members. Equivalence between the proportion of a member’s contributions and the benefits which he enjoys is of no moment

as long as there is payment by him for the repeated use of its facilities available to the members. Plaintiff is such an association.

“To constitute a club within the meaning of Section 101(9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity. Plaintiff meets these requirements.

“Plaintiff association is and was at all times here pertinent a club within the meaning of Section 101(9) of the Internal Revenue Code.

“A club operated for pleasure or recreation is one in which the members carry out or enjoy those common purposes acting either individually or collectively. Plaintiff association is such a club.

“Specific activities and services of Plaintiff which if performed by others might be deemed of a commercial or profitable nature are, as carried on by Plaintiff, performed for purposes of pleasure and recreation of its members and not for profit.

“The mere receipt of money, by an organization exempt under Section 101(9) of the Internal Revenue Code, as a result of incidental activities, or in insignificant amounts, is not sufficient to destroy the exemption under that Section so long as the money is expended for exempt purposes. It is the destination and not the source of the income which governs the right to exemption.

“The Plaintiff association was not organized or operated for the purpose of making a profit or

building up a surplus for the benefit of itself or its members.

“Neither the pleasure and recreation nor the non-profitable nature of Plaintiff’s objectives and purposes is destroyed by its members’ occasional use of its facilities and services for their individual business purposes.

“The excess of receipts over expenditures of Plaintiff association resulting from the unavoidable curtailment of Plaintiff’s services during any year did not constitute ‘net earnings’ within the meaning of Section 101(9) of the Internal Revenue Code, and did not inure to the benefit of any member of Plaintiff.

“Non-profitable purposes within the meaning of Section 101(9) of the Internal Revenue Code are not changed to profitable purposes by the mere fact that in some years the receipts of Plaintiff exceeded its expenditures.

“Plaintiff association was organized and operated exclusively for pleasure, recreation and other non-profitable purposes during the years 1943 and 1944.

“No part of the net earnings of Plaintiff association inured to the benefit of any of its members during the years 1943 and 1944.

“Plaintiff is entitled to judgment as prayed.”

It may be noted at this point that after the submission by appellee to the District Court of proposed findings of fact and conclusions of law, no objections thereto or suggestions for change in any respect were filed by the Government in opposition to such proposed findings or conclusions.

SUMMARY OF ARGUMENT.

Appellee was at all times, including the years 1943 and 1944, a "club" within the meaning of Section 101(9) of the Internal Revenue Code, as well as under the practically identical provisions of all Revenue Acts beginning with that of 1916, down to date. In a club of this nature, and in this particular club, neither social intercourse nor commingling of members is necessary, although, as will later be shown, there was commingling of members in annual meetings, periodical meetings of its board of directors, and in connection with the meetings and activities of ten standing committees, etc. (R. 178.) Appellee comes squarely within a number of definitions, which will be cited herein, of the term "club". Appellee also meets the terms of the statute that it be organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, and that no part of its net earnings inures to the benefit of any member.

The District Court, in separate findings, has held that appellee meets all the requirements of Section 101(9).

A. HISTORY OF SECTION 101 (9) OF THE INTERNAL REVENUE CODE.

The section in question during the years 1943 and 1944, as well as prior and subsequent thereto, provided as follows:

"Section 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

“The following organizations shall be exempt from taxation under this chapter—

* * * * *

“(9) Clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.”

The Revenue Act of 1913 was the first Income Tax Act under the 16th Amendment, but it provided that the income tax should not apply to:

“* * * any corporation or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of the net income of which inures to the benefit of any private stockholder or individual, nor to business leagues, nor to chambers of commerce or boards of trade, not organized for profit or no part of the net income of which inures to the benefit of the private stockholder or individual; nor to any civic league or organization not organized for profit, but operated exclusively for the promotion of social welfare; * * *.”

The foregoing exclusions of the 1913 Act did not specifically include a club of the type of appellee, but in spite of that fact, the Commissioner of Internal Revenue did not impose any income tax upon appellee under that Act.

Section 11(a) of the Revenue Act of 1916, which was the next Revenue Act after that of 1913, provided exemption from income tax of:

“Ninth. Clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net income of which inures to the benefit of any private stockholder or member.”

It will readily be observed that, except for the change of several unimportant words in the section just quoted, the same provision of law has continued to grant exemption to the clubs described from 1916 down to the present time.

Identical language to that of the 1916 Act was contained in the Revenue Act of 1918, and such exemption was provided in the Revenue Act of 1921 in the same language.

The Revenue Act of 1924, Section 231(9), gave the same exemption but changed the wording very slightly from “private stockholder or member” to “private shareholder”, as it is today.

The same identical language as used in the 1924 Act, providing income tax exemption to such clubs, is found in each subsequent Federal Revenue Act to and including the Revenue Act of 1938, and identical wording is found in the present codification of revenue laws called the Internal Revenue Code. In fact the exempting provision has been enacted by Congress eleven times.

Throughout its existence, since the inception of the income tax in 1913 down to the year 1943, appellee had never been required by the Federal Government to pay, nor had it paid, any income or excess profits

taxes. It was, therefore, considered by the Government to be exempt from taxation for a period of thirty (30) years, and the Commissioner of Internal Revenue did not seek to subject it to taxation until his first ruling letter to that effect, dated September 23, 1944 (Exhibit 1-B).

B. APPELLEE IS A "CLUB" WITHIN THE MEANING OF SECTION 101(9) OF THE INTERNAL REVENUE CODE.

The New International Encyclopedia, Volume 5, pages 487 et seq., defines the word "club" as follows:

"A word said to be derived from the Saxon cleofan, to divide—a club being an association the expenses of which are shared among the members."

"*The Automobile Club of America*, devoted to the advancement and regulation of motoring was established in 1890 and has 1,660 members. *The Aero Club of America*, founded in 1906 for the promotion of aeronautics, now has 340 members." (Italics supplied.)

It is important to note that the foregoing definition cites *The Automobile Club of America* as its first illustration of a "club".

The following judicial construction of the term "club" is pertinent and illuminating:

"The subdivision of lake frontage land, under which purchasers of lots were to have common or community rights to lake frontage bathing and boating privileges, and water supply, was held a violation of covenants prohibiting its use for

‘club’ purposes; a ‘club’ meaning a combination or association formed to combine the operation of persons interested in the promotion or prosecution of some object, and as used in the covenant, including clubs of all kinds.”

Robert v. Gerber, 202 N. W. 701, 703, 187 Wis. 282.

“A club is an association of individuals for pleasure or profit.”

Martin v. State, 59 Ala. 34.

“The word ‘club’ has no very definite meaning. Clubs are formed for all sorts of purposes, and then in no uniformity in their constitution and rules.”

Commonwealth v. Pomphret, 137 Mass. 564, 567.

Webster’s New International Dictionary sets forth, among other definitions of the word “club,” the following:

“To unite for a common end, or contribute to a common stock; as to club exertions. * * *”

Intransitive—“to form a club; to combine for the promotion of some common object; to unite.”

Webster’s same dictionary, Second Edition, Unabridged, in defining the word “association” gives the following synonyms:

“company, fellowship, body, league—association, society, club—agree in the idea of a *body of persons united in the interest of a common object*. Association and society are practically interchangeable, the Young Men’s Christian Associa-

tion, the Christian Endeavor Society, The American Historical Association, The Philological Society. Frequently, however, association suggests a somewhat larger inclusiveness than society, whether with regard to the objects of the organization or to the persons admitted to membership. A club is usually a more private body than either of the others and is often purely social." (Italics supplied.)

The Commissioner of Internal Revenue himself, in letters addressed to appellee, dated January 25, 1945, and August 21, 1945 (Exhibits 2-A and 2-C), dealing with the capital stock tax returns of appellee for the years ending June 30, 1944, and June 30, 1943, respectively, refers to the former bureau rulings of September 23, 1944 (Exhibit 1-E), and July 27, 1945 (Exhibit 1-G), that appellee would be required to file returns of income, and twice uses the expression:

"* * * *that automobile clubs such as yours, which are within the scope of the Bureau rulings, will not be required to file returns of income for years beginning prior to January 1, 1943.*" (Italics supplied.)

Those two letters not only plainly characterize appellee as an *automobile club*, but are also directly connected with the rulings of the Commissioner with reference to filing income tax returns, as they specifically refer to such rulings.

The foregoing rulings, Exhibits 2-A and 2-C, are pertinent for the further reason that a capital stock tax was due in 1943 and 1944 only if a corporation was

subject to the income tax, and if a corporation was exempt from income tax it was then also exempt from the capital stock tax. Section 1201 of the Internal Revenue Code demonstrates this point. It read as follows, before its elimination from the code as to years ending after June 30, 1945:

“(a) The taxes imposed by Section 1200 shall not apply—

“(1) CORPORATIONS EXEMPT FROM INCOME TAX
—to any corporation enumerated in Section 101;
* * *”

Likewise, an excess profits tax was payable in 1943 and 1944 only if a corporation was subject to income tax.

Furthermore, in the final ruling of the Commissioner of Internal Revenue himself, in a letter dated July 27, 1945, to appellee (Exhibit 1-G), the Commissioner refers to “automobile clubs” in the following language:

“Prior to the time that the information submitted by you in 1941, was taken up for consideration a substantial number of *automobile clubs* had been held to be entitled to exemption under Section 101(9) of the Internal Revenue Code and prior revenue acts. While the information submitted by you was under consideration in this office, it was decided to reexamine the general question of whether *an automobile club or association* having the usual purposes and activities is entitled to the exemption provided in Section 101(9) in connection with a particular case, and in G.C.M. 23688 (C.B. 1943, 283) it was con-

cluded for the reasons therein stated that the subject automobile association is not entitled to the exemption. * * *” (Italics supplied.)

Thus the Commissioner has a number of times called appellee itself, as well as similar organizations, an “automobile club”.

In *Portland Cooperative Labor Temple Association v. Commissioner of Internal Revenue*, 39 B.T.A. 450, petitioner contended that it was exempt from income and excess profits taxes under Section 101(1) granting exemption to labor, agricultural and horticultural organizations. Speaking of the term “labor organization”, the Board said:

“The term has been used continuously for 30 years to bestow tax exemption, and it never has been found desirable by Congress to qualify it or by the administrator to give it a narrowing interpretation. There is no occasion to attempt a definition now. It bespeaks a liberal construction to embrace the common acceptance of the term, including labor unions and councils and the groups which are ordinarily organized to protect and promote the interests of labor. The petitioner, we think, was within such a category during the years 1934 and 1935, and was therefore exempt from tax.”

On page 7 of appellant’s brief, in support of its contention that appellee is not a club, the following statement appears:

“In the absence of a statutory definition or helpful legislative history it seems appropriate to

conclude that Congress intended by the section to exempt organizations which are usually and commonly referred to as clubs."

While the criterion suggested by the Government in the language just quoted is by no means exclusive, as is indicated by the definitions of the term "club", *infra*, appellant has apparently unwittingly added strength to appellee's contention by referring to *exempt* organizations which are *usually and commonly referred to as clubs*, in view of the fact that as a matter of common knowledge the term "automobile club" is quite universally used to describe an organization such as appellee. Many of them actually have the word "club" included within their official names, such as the Automobile Club of Southern California.

Also in the definitions of the word "club" on the same page of appellant's brief there is reference in each definition to the promotion or pursuance of some common object. There can, we believe, be no denial of the statement that the members of taxpayer were banded together for the promotion of the objectives set forth in the findings of fact of the District Court (R. 82-84), which collectively clearly constitute a "common object".

The definitions from Webster's New International Dictionary and from Funk and Wagnalls' New Standard Dictionary quoted by appellant on page 7 of his brief define the word "club" in a manner which is helpful to appellee. Certainly the appellee is "an association of persons for the promotion of some

common object * * *” or objects, being those objects and purposes described in detail, *infra*. The further definition that membership in a club is “usually” conferred by ballot certainly does not preclude the existence of a club in which membership is not so conferred. For example, in G.C.M. 22116, C.B. 1940-2, page 100, granting exemption to a college alumni association under Section 101(9), membership in the association was not limited in number and the members were not selected by ballot. Anyone who received a degree from the college or who was in any way connected with the college even though not the recipient of a degree, was eligible for membership upon payment of regular annual dues. This ruling is still in effect and clearly shows that even the Bureau of Internal Revenue does not adhere to the argument made in the Government’s brief in construing the statute.

In addition, in O.D. 280, C.B. 1919, page 203, the Bureau of Internal Revenue held that a political club was exempt under this same statute. That ruling is still in effect and likewise clearly shows that the Bureau has never imposed the requirements of limited membership or membership conferred by ballot as a requirement for exemption.

Furthermore, other and more numerous dictionary definitions, as well as judicial definitions of the term “club”, which have hereinbefore been cited in support of appellee’s contention that it is a club, do not lay down any such conditions as set forth in appellant’s brief.

The District Court has found as a fact "That Plaintiff association is a club" (R. 86).

Appellant's statement on page 8 that appellee has no clubhouse or other meeting place is not in accord with the facts as appellee not only must have a place for its annual meetings, but also has a large headquarters building at 150 Van Ness Avenue, San Francisco, together with thirty-five (35) branch offices scattered throughout the territory which it serves. Members not only can, but do, meet and particularly at its headquarters, where its Board of Directors and its numerous committees meet both periodically and specially for the transaction of business in the interest of the entire membership.

Also on page 8 of its brief, appellant pointed out that the Court below concluded that (R. 87) "A club is an association the expenses of which are shared among its members," and also concluded that (R. 87) "To constitute a club within the meaning of Section 101(9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity." In its last quotation appellant omitted the final sentence of the District Court's conclusion, which reads "Plaintiff meets these requirements."

Appellant then says that he finds no support for the conclusion that the mere sharing of expenses among

individuals gives to the group the aspect of a club, but he fails to take into account the conclusion of the Court below, just above quoted, which obviously expands the Court's preceding finding that "A club is an association the expenses of which are shared among its members," and furnishes additional reasons for the Court's ultimate conclusion that appellee is a club.

Appellant admits on page 8 of his brief that the use of the word "club" does not *necessarily* carry with it the idea of social intercourse. That is exactly what appellee contends and what the Court below has found (R. 87).

It is observed that there are two quite important omissions on page 9 of appellant's brief where it is said that "It is difficult to understand what the lower Court had in mind by saying that 'it is sufficient if its members make a common cause in a financial * * * sense' " (R. 87). That excerpt is taken from Conclusion II just above referred to (R. 87), which appears on page 8 of appellant's brief, and while only the two words "or other" are omitted where the three asterisks appear, it is obvious that such omission restricts the meaning of the lower Court's conclusion in a manner which was clearly not intended by that Court. The words "or other" cover the numerous ways in which the members of a club under Section 101(9) operate as a club, and naturally include the variety of other activities of the appellee which collectively, in the judgment of the lower Court, qualify it as a club. It would seem that nothing was to be

gained by the omission of the two words "or other" and the substitution therefor of the three asterisks, except to provide a basis for an argument that taxpayer could not be a club if its members merely make a common cause in a financial sense. The lower Court did not so restrict its findings.

The other noteworthy omission by appellant is the phrase "or if there is present group activity" which immediately, and as part of the same sentence, follows "in a financial or other sense". To all this should be added the concluding sentence used by the Court, "Plaintiff meets these requirements."

Appellant did not indicate that another phrase followed the word "sense" in his quotation on page 9 of his brief, and that another complete sentence was also omitted. The result has been to distort both the content and the meaning of the District Court's conclusion.

Appellant is completely in error in several assertions he has made in the second paragraph on page 9 of his brief, especially where he says that "The entire record clearly shows that taxpayer has no activities commonly associated with club functions," and that if a motorist thinks about joining an association of the type of appellee "his first and only consideration is whether or not the services and reduced insurance rates are worth the dues he will be required to pay". It is believed that the first statement above quoted is completely refuted by "the entire record" to which appellant refers, and the findings of the lower Court

which show that appellee has an organization typical of many clubs in that it has executive officers, a board of directors, a considerable number (ten) of functioning committees, a dues-paying membership, annual meetings which all members are invited to attend, pursuit of a common objective, etc. The second quoted statement of appellant is likewise refuted by the record, including the finding of the lower Court that appellee is a separate and distinct organization from the California State Automobile Association Inter-Insurance Bureau (R. 86); that appellee does not and never has maintained or operated an insurance bureau, department or other agency for the placing of automobile insurance; that the right to obtain insurance through the Inter-Insurance Bureau is not open to all members of appellee, but is restricted to selected individuals who must meet certain qualifications and who are not entitled to so obtain insurance if they have a record of hazardous driving, a bad insurance record, etc. Furthermore, appellee's members are not required to become subscribers of the Inter-Insurance Bureau (R. 126, 127, 140, 141, 183). In addition, there is no certainty that insurance will cost an insured under the Inter-Insurance Bureau less than it would in non-board or conference companies, or in other cooperative insurance concerns (R. 141).

On pages 10, 11 and 12 of appellant's brief there are quotations from and discussion of G.C.M. 23688, 1943 C.B. 283, a memorandum issued by the chief counsel of the Bureau of Internal Revenue, which memorandum overrules or modifies a number of other rulings of

many years' standing. The subject of discussion in that memorandum is obviously a *nation-wide federation of automobile clubs*, as is evident from the last two paragraphs on page 1 thereof, where the M Association is stated to function to a large extent as a "federation of automobile clubs" and as "the managing agency of several local automobile clubs," and referring also to the fact that membership in that club is confined to "(a) State Associations, (b) automobile clubs, (c) automobile divisions, (d) commercial vehicle organizations." Although the Bureau of Internal Revenue, in conformity with its consistent practice uses merely a letter to identify the "M Association", the foregoing description points strongly to the assumption that the subject of the memorandum is the American Automobile Association.

And on page 2 of said memorandum we find that "individuals who are, or become,, affiliated with this corporation *shall not be members*, but shall be classed as regular and honorary associates * * *." (Italics supplied.)

The M Association is wholly unlike appellee, as the latter, whose activities are set out in the present record, does not function as a federation of automobile clubs or as a managing agency of local automobile clubs, nor does it conduct or participate in any such functions. Likewise, it does not organize, supervise, or grant affiliation to other corporations, associations, or organizations with similar objects and purposes, as described in paragraph (f) of the by-laws of M Association. Appellee has no member clubs and does not

in any sense operate as a federation of automobile clubs.

Appellee is sharply distinguished from the M Association also in that it bears no resemblance whatsoever to the organization described in G.C.M. 23688, whereby "Arrangements have also been made with certain merchants in one area whereby members of one of the local organizations may purchase clothing, laundry, furniture, and automobile supplies at less than the usual selling prices of such articles." Appellee does none of these things (R. 175).

Another difference between appellee and the M Association is that in the latter, individual members as such have no right to vote in the affairs of the corporation (page 2, paragraph 4), whereas in appellee the individual members have both of such rights, and the record shows that they do vote and otherwise actively participate in the affairs of the corporation. Likewise, appellee, unlike the M Association, does consist of members who participate in activities looking to the rendition of the services offered by appellee, all of which are designed to and do contribute to the pleasure and recreation of the membership.

Again, there is a radical difference between appellee and the M Association, which latter is stated in G.C.M. 23688 to operate "in the nature of a non-profit cooperative buying association," as appellee indulges in no such activities whatever. Furthermore, appellee is not itself, nor does it perform any of the functions of, a "commercial vehicle organization", as does the M Association.

A comparison of the activities and operations of appellee and M Association show it to be widely divergent from the latter in practically every respect.

The record indicates either affirmatively as to certain activities of appellee, or negatively as to others, that appellee did not engage in a number of the activities attributed to the M Association.

In this connection attention is invited to the admission of appellant that appellee "did everything that is in the record here that they did do, and did nothing else" (R. 175). (*Italics supplied.*)

The great differences between appellee's activities, as shown by the record, and the activities and purposes of the M Association as shown in G.C.M. 23688, *infra*, weaken materially the force of the Commissioner's final ruling of July 27, 1945, Exhibit 1-G (R. 17), in which it is stated that "in G.C.M. 23688 (C.B. 1943, 283) it was concluded for the reasons therein stated that the subject automobile association is not entitled to the exemption. This opinion was first published during the first part of July, 1943, after which the information submitted by you during October, 1941, was again taken up for consideration *in the light of the view expressed in that General Counsel's Memorandum*, and it was concluded with the concurrence of the chief counsel and the approval of the then acting secretary of the treasury, that you are not entitled to the exemption provided in Section 101(9) * * *." It is submitted that G.C.M. 23688 has no proper application to the case at bar. (*Italics supplied.*)

It is also quite interesting to note that the same chief counsel of the Bureau of Internal Revenue, J. P. Wenchel, who issued G.C.M. 23688, *infra*, also issued G.C.M. 22116, 1940-2, CB 100, *infra*, holding that the M Alumni Association was exempt from tax under Section 101(9) of the Code. It was stated to be organized primarily to promote in every proper way the interests of the M College and to foster among its graduates a sentiment of regard for each other and attachment to their alma mater. The purposes of M Alumni Association included the following: "To raise money by subscriptions, and to grant any rights and privileges to subscribers." The chief counsel stated that "Other income is derived from the sale of advertising space in the magazine and a small amount of interest is received from a fund composed of paid life membership fees. The income is used to defray operating expenses of the association, and any balance over expenses is given annually to the college to be applied to some need." No mention whatever is made of any pleasure or recreation purposes, nevertheless exemption from income taxation under Section 101(9) of the Code was granted.

In I.T. 2693, XII-1 C.B. 59, income tax exemption was allowed a club incorporated with the declared purpose of making trails and roads in certain mountains, to erect camps and shelter houses therein, to furnish maps and guide books, and to make these mountains play a larger part in the life of the people. Its income is from dues and the sale of maps, guide books and similar publications and no part inures to the benefit

of any private individual. This ruling was based upon the same reasoning as that upon which some of the earlier automobile club rulings were predicated, but revoked in G.C.M. 23688, *infra*, but I.T. 2693 has not been revoked or rescinded and apparently therefore still stands.

Appellant says that appellee association does not provide for commingling of members in fellowship and hence is not a club. It apparently bases such assertion upon some of the language dealing specifically with the excise tax, under Section 1710 of the Code, imposed on a "social, athletic, or sporting club or organization," and applicable only to that type of club and not to clubs mentioned in Section 101(9). Such commingling is not required as an element in the definition of a club under the latter section, or under the regulations issued in connection therewith.

We cannot agree with appellant's statement on page 8 of his brief implying that a club must have a clubhouse. It is a far stretch of credulity to suppose that Congress intended the tax exemption under Section 101(9) to turn upon the kind of physical facilities possessed by the organization.

The Commissioner's final adverse ruling of July 27, 1945 (Exhibit 1-G) (R. 15) shows that such ruling was largely predicated upon G.C.M. 23688, *infra*, which we submit has no proper application, and upon the assertion that appellee was not a club under the decision in *Arner v. Rogan*, cited and discussed in G.C.M. 23688, and on pages 10, 11 and 12 of appellant's brief.

Arner v. Rogan dealt with the question of the application of the *excise* tax under Section 501 of the Revenue Act of 1926 to a *social, athletic or sporting club*, and not to the exemption from *income* tax of a club such as taxpayer under Section 101(9) of the Code. Section 501 of the Revenue Act of 1926 was the predecessor and counterpart of Section 1710 of the Internal Revenue Code, which is found under Chapter 10, *Admissions and Dues*, while Section 101(9) is found in Chapter 1, *Income Tax*.

Section 1710 *imposes* an *excise* tax upon dues and membership fees of a specifically described type of club, wholly unlike the clubs described in Section 101(9), which section *exempts* the same from *income* tax.

There is, therefore, in the tax treatment of the divergent types of clubs respectively dealt with in Sections 1710 and 101(9) no necessary or natural connection, and the descriptions of these two distinctive groups of clubs add further emphasis to the fact that the two sections of the Code mentioned are not only not identical, either in description or purpose, but that the only thing they have in common is the generic term "club".

There is no reference whatever in Section 101(9) to social, athletic, or sporting clubs, which are the sole objects of taxation under Section 1710, and it is obvious from the most cursory consideration of the terms "pleasure" and "recreation" that certain forms of both pleasure and recreation may be indulged in by

persons acting individually and with no association whatever with other individuals.

In *Better Business Bureau v. United States*, 326 U. S. 279, the Supreme Court carefully noted that Congress has written a slightly different definition into the Social Security Act than in the Income Tax Act, and said that this indicates an intention on the part of Congress to make a demarcation between certain types of corporations. The same reasoning applies to the distinction made by Congress by defining, in Section 101(9), clubs organized and operated exclusively for pleasure, recreation and other non-profitable purposes, as distinguished from social, athletic or sporting clubs, which are required to pay an excise tax under 1710 of the Code.

The pertinent language of the Supreme Court in this connection follows:

“* * * And Congress had made it clear, from its committee reports, that it meant to include within Section 811(b) (8) only those organizations exempt from the income tax under Section 101(6). Significantly, however, Congress did not write into the Social Security Act certain other exemptions embodied in the income tax provisions, especially the exemption in Section 101(7) of ‘business leagues, chambers of commerce, real estate boards, or boards of trade’. Petitioner closely resembles such organizations and has, indeed, secured an exemption from the income tax under Section 101(7) as a business league. Thus Congress had made, *for income tax exemption purposes*, an unmistakable demarcation between corporations or-

ganized and operated exclusively for educational purposes and those organizations in the nature of business leagues and the like. Its manifest desire to include only the former within the meaning of Section 811(b) (8) of the Social Security Act prevents us from construing the language of that section to include an organization like petitioner.
 * * *” (Italics supplied.)

Referring to the quotation in G.C.M. 23688, *infra*, from *Arner v. Rogan* by appellant on page 11 of his brief:

“* * * at least there must be some sort of association or cooperation between the members in an effort to reach some common objective before we may consider that there is a club or organization,”

it may be stated, unequivocally, that as the record shows, there is both association and cooperation between the members of appellee “in an effort to reach some common objective,” so that in fact the quotation from *Arner v. Rogan*, upon which appellant relies, is in support of appellee’s contention. The whole purpose of the organization and operation of appellee was to provide the necessary association and cooperation among its members for the achievement of its objective, namely, the pleasure and recreation of the passenger car owners constituting its membership, by the improvement and marking of roads, obtaining legislation to further the construction of more and better highways, providing a quick and efficient towing service to members in distress on the highways, furnishing travel information and guides to its members, etc.

Quite significantly the Court also said in *Arner v. Rogan*:

“There never was any general corporate meeting of any kind and one man seemed to determine all questions even without reference to a Board of Directors and apparently without any express authority to do so. The only evidence of any intention to give members any control is contained in the various pieces of literature which were apparently handed out by the manager, or sent out by the manager, and, according to his testimony, the only purpose thereof was advertising. The evidence shows that members never met together or in committee and never participated in any activities which are normally carried on by members of clubs or similar organizations, nor is there evidence that the patrons were entitled by the terms of their contracts to so participate.” (Italics supplied.)

It may be pertinent again to point out that the members of appellee association, through collective action, regularly elect a board of directors, made up of twenty-one members of the association, which meets both regularly and specially throughout the year. It has ten committees, enumerated in the record, and to which a considerable number of members, in the aggregate, are appointed. Other members of appellee attend special committee meetings, such as those of the legislative committee, although not members of that committee. The members of appellee are invited and urged to and do attend and participate in the annual meetings of the association. All of the committee work and other activities are designed to further, through asso-

ciation and cooperation among the members, the common objectives of appellee, which obviously could not be achieved except through such collective action. Appellee therefore meets the very requirements laid down by the Court in *Arner v. Rogan*.

It is significant to note that while the section of the regulations issued by the Commissioner under Section 101(9) bears the title "Social Clubs", it is *not* restricted to such clubs, but specifically provides that in addition thereto the exemption granted by Section 101(9) applies to practically all recreation clubs supported by membership fees, dues, and assessments.

Of special significance is the fact that under the regulations promulgated under the various revenue acts preceding the establishment of the Internal Revenue Code, as well as the similar section under the code itself—Section 101(9)—the article or section of such regulations has been headed "Social Clubs", obviously for the purpose of brevity, although from the context of the regulations, beginning with those under the Revenue Act of 1916 (Regulations 33), it is quite clear that recreation clubs supported by membership fees, dues and assessments (as is the appellee), are included in the exemption along with so-called social clubs. It could not be otherwise, in fact, as the regulations can only carry out the intent of Congress in defining the types of clubs to be granted exemption, and cannot restrict the types so enumerated. The first regulations on the section under discussion are found in Art. 72, Regulations 33, under the Revenue Act of 1916, and read as follows:

“Social Clubs. Social clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes are exempt from the tax, provided no part of any net income which they receive inures to the benefit of any private stockholder or individual. This exemption will reach practically all social and recreation clubs which are supported by membership fees, dues, and assessments.”

However, under Art. 520 of Regulations 45, under the Revenue Act of 1918, the context did not stress social clubs as it did under Regulations 33, *supra*, but reads: “The exemption applies to practically all social and recreation clubs * * *,” which terminology has been carried throughout the regulations under the various legislative provisions in the Revenue Acts and the code dealing with the exemption here under consideration, and the latest regulations under Section 101(9)—Regulations 111, Section 19. 101(9)—provide as follows:

“Social Clubs. The exemption granted by Section 101(9) applies to practically all social and recreation clubs which are supported by membership fees, dues, and assessments. If a club engaged in traffic, in agriculture or horticulture, or in the sale of real estate, timber, etc., for profit, such club is not organized and operated exclusively for *pleasure, recreation, or social purposes*. *Generally, an incidental sale of property will not* deprive the club of the exemption.” (Italics supplied.)

The regulations have not been changed since 1937, although there have been several reenactments of Sec-

tion 101(9) since then, without change. Therefore, there is no basis in the regulations for the position taken by the Commissioner that appellee is no longer exempt.

In *Bryant v. Commissioner*, 111 Fed. (2d) 9, decided by this Court, and reversing the Board of Tax Appeals, the question was whether interest paid Mrs. Bryant on street improvement bonds of the city of Los Angeles was tax exempt. The administrative practice at least until 1936, or for more than 22 years, was to treat as within the statutory exemption interest upon bonds which were not general obligations of the issuing political subdivision but were payable only out of a particular fund. In 1936, two years after the tax there involved, a contrary opinion was expressed in a general counsel's memorandum. The Court said:

"The established administrative practice of so many years, during which time the exemption was several times reenacted, carries weight as a construction of the statute which is not offset, at least as to the tax year in question, by the later expression of opinion in G.C.M. 16861, XV-2 Cum. Bull. 179 (1936)." (Italics supplied.)

In *Citizens National Trust & Savings Bank of Los Angeles v. United States*, 135 Fed. (2d) 527 (CCA-9), the bank contended that R. S. 3186 gave the United States a lien only upon property possessed by the taxpayer at the time of the distraint and that the lien did not attach to after-acquired property. This Court held that the statute, by its terms, applied to after-acquired property but went on to say that if the statute was so

general in its terms that an administrative interpretation was appropriate, the statute had been interpreted to apply to after-acquired property. Since such interpretation the section had been twice amended with no addition of a definite provision as to after-acquired property and presumably with Congressional knowledge of the departmental interpretation. The Court said: "Therefore, such interpretation must be taken as approved by Congress."

Furthermore, it is of the greatest significance that the Bureau of Internal Revenue for a period of 30 years, from 1913 to 1943, under these very regulations, even though entitled "Social Clubs", consistently exempted appellee from income taxation. Other automobile clubs were also so exempted. G.C.M. 23688, *infra*. It is clear, therefore, that appellee is not required to qualify as a social club under Section 1710 of the Code in order to entitle it to exemption under Section 101(9).

C. APPELLEE WAS ORGANIZED AND OPERATED EXCLUSIVELY FOR PLEASURE, RECREATION, AND OTHER NON-PROFITABLE PURPOSES.

It is important first to determine the full meaning of the words "pleasure" and "recreation", as both words have definitions and synonyms which enlarge the scope of meaning conveyed by the mere words themselves.

Roget's International Thesaurus, in defining the word "pleasure", includes the synonyms, "gratifica-

tion", "enjoyment", "well-being", "satisfaction", "happiness", "joy", "cheerfulness", and "pleasant time".

The same authority in defining the word "recreation" gives the synonyms "amusing", "entertaining", and "diverting".

Webster's dictionary of synonyms for each of the words "pleasure" and "recreation" includes several of those found in Roget.

In *National Surety Company v. Jarrett*, 121 S.E. 291, 295, 95 W. Va. 420, it is said that "'pleasure' is synonymous with comfort, consolation, contentment, ease, enjoyment, happiness and satisfaction."

In *Committee for Industrial Organization v. Hague*, D.C.N.J., 25 F. Supp. 127, 145, it is stated that "the purpose of most parks is the 'recreation' of the public, including not only physical recreation, but mental recreation, * * *."

It may be somewhat difficult in these days of wide, smooth, well-constructed concrete highways, so amply marked by road signs that an automobile traveler may be kept informed as to his location, the name and distance of the next town or city, where he should make a necessary turn, and even the condition of the highway if a portion farther on is under repair or construction, to project one's thoughts back to the days of 1907 when appellee was first organized, and to 1913 when, as David E. Watkins (secretary and general manager of appellee since that year) testified (R. 148, 149), the condition of the roads was "deplorable",

meaning, what we believe to be a matter of common knowledge, that there were practically no hard-surfaced highways, the roads were usually very narrow, dusty during dry weather, rutted and slippery in wet weather, when it was difficult for two vehicles to pass each other without, in many cases, endangering safety by getting off into a ditch and causing great inconvenience, discomfort and, in many cases, some type of casualty. In 1907 the automobile was new, it had been in even very limited use only for a few years, and was being used practically exclusively for pleasure purposes. The automobiles themselves at that early date were, to some extent, experimental in nature and construction, and were subject to frequent breakdowns on the road, particularly under the highly unfavorable road conditions which then existed.

It was in the light of such an unfavorable state of affairs, which are a matter of common knowledge, that the incorporators of appellee got together to form an organization for the purpose of improving road and other conditions so as to make the use of pleasure cars safer and more enjoyable, thus contributing materially to the "comfort", "contentment", "enjoyment", "satisfaction" and pleasure of their owners, and to further the opportunities for recreation which such improved conditions would provide, including easier and safer access to mountains, lakes and other recreation spots.

Even a cursory glance at the purposes set forth in appellee's Articles of Incorporation on August 30, 1907, will show that they were all designed to promote the pleasure and recreation of its members:

“Throughout the State of California and elsewhere,
 To promote the improvement of the highways;
 To encourage proper highway maintenance;
 To accomplish the proper marking of the highways;
 To urge just and rational highway legislation;
 To further all good roads projects;
 To protect the legitimate interests of members;
 To affiliate or associate with itself similar associations;
 To promote speed and endurance contests for motor vehicles;
 To purchase, hold and convey real and personal property as its purposes may require.”
 (Ex. 1-A.)

Throughout its history, appellee has adhered to the purposes thus set forth in its articles of incorporation, and its whole plan and purpose has been a constant endeavor to secure the improvement of highways, including the function of road signing, and the other activities set forth in the evidence in this case, so that its members would progressively be furnished with all the aid and assistance which could be made available to contribute to their pleasure and recreation in the use of their pleasure cars. There has been no change in the type of appellee corporation as originally organized.

As the evidence further shows, appellee during the years 1943 and 1944, as well as prior and subsequent

thereto, has furnished, among other services, the following:

Emergency road service, including towing service, for the aid and assistance of its members who may encounter trouble of any kind with their automobiles while on the highways, such service being restricted, however, to passenger cars (R. 123, 124, 128-132).

Claim adjustment service for the convenience and comfort of its members when they were involved in accidents, in adjusting the matter of damages, including adjustments made with municipalities for infractions of traffic regulations, etc. (R. 131, 132).

Investigating, listing and publishing, for the benefit of its membership, the names of accredited hotels, lodges, restaurants, etc., where appellee's members might rely upon obtaining satisfactory and adequate lodging, and meals, thus contributing to their comfort, well-being and pleasure, and relieving them of anxiety as to whether certain stopping places were safe and reliable (R. 167, 168, 198).

The erection, repair and maintenance, at its own expense, with the exception of the actual cost of materials, of road signs, including parking signs, direction signs, distance signs, restriction signs, signs for cities, towns and resorts, and for places of historical interest, as well as signs containing information as to local ordinances and regulations, danger and detour signs, etc. In connection with such road signing, appellee spent large sums of money for which it was not reimbursed. No one else has done such road signing

in appellee's territory since the latter began it in 1914, and appellee started it for the recreational convenience and pleasure of its members (R. 170, 192-194).

Appellee's chief engineer, James W. Johnson, is a member of the Joint Committee on Uniform Traffic Control Devices which holds regular meetings in Washington, D. C., and which designs traffic devices (R. 195).

The publication of a monthly magazine, "Motorland", issued as one of the incidents of membership, without further cost, each month to all the members of appellee to keep them advised not only of the activities of their association but of all matters of interest arising in connection with the operation of their automobiles. While in earlier years appellee had some income from advertising in said magazine, such income was entirely eliminated late in 1941 and there was no such income in 1943 and 1944 (R. 161-164).

The issuance of licenses by appellee's touring bureau under arrangements with the State of California by which a block of licenses each year is assigned to appellee for distribution to its members. Such distribution eliminates the waste of time and inconvenience involved in standing in line at State automobile registration offices and enables appellee's members to obtain their annual licenses with a minimum of inconvenience and discomfort (R. 199).

One of the most important and one of the most widely used of the services offered by appellee to its membership is its touring service. Through its touring

bureau, members obtain a wide variety of information, particularly for use in connection with contemplated trips for pleasure and recreation. A very large number of maps are distributed to appellee's members through the touring bureau, including state and sectional maps, maps of various Western States and highways, strip maps, etc. Lists of hotels, lodgings, and restaurants distributed to its members cover not only the Western United States but the entire country and Canada as well. The touring bureau also furnishes a large volume of information to members planning vacation trips, including places to stay, roads to take, highway conditions, facilities for camping, fishing and hunting conditions, including information as to open and closed seasons, etc. During the past five years, the average number of calls for such information which have been answered by the touring bureau was a minimum of 500,000 inquiries each year (R. 197-201). In that connection, it is interesting to note, as shown on page 25 of the statement attached to appellee's several claims for refund, appellant's Exhibits A and B, that in the year 1940 the report of the president contained a detailed statement of services rendered by its touring bureau, including the furnishing of information to practically 200,000 motor touring parties, preparation of 19,000 transcontinental routings, and 30,000 other out-of-state routings, the issuance of more than 367,000 road maps, and the handling of over 170,000 telephone requests from members seeking travel information, exclusive of thousands of such inquiries received by San Francisco headquarters and not tabulated.

For many years appellee has maintained a public relations department, including its public safety work, its highway activities, and legislative activities. At its own expense, starting at the kindergarten level and up through the various grades of elementary schools and into high schools and colleges, appellee has sponsored, developed, prepared and distributed large quantities of materials for safety educational work. It sponsored and developed the idea of school safety patrols in 1923; it has published and furnished, free of charge, publications dealing with safe driving, driver training, and other subjects, and has prepared and distributed vast numbers of safety posters and safety lessons. Appellee has also established a traffic survey service available to communities without charge, and assists such communities in putting its recommendations into effect (R. 133, 202-208).

One of its important activities, and one included in its original Articles of Incorporation, has been the development and recommendation of adequate, sound, motor vehicle legislation, and sound and adequate highway improvement programs. It has sought appropriate legislation not only from the State legislature but from municipalities and counties as well (R. 208, 209).

Appellee has promoted a uniform traffic code for all cities within its territory. In 1943 and 1944, it sponsored the National Pedestrian Protection Contest. It has carried on weekly radio programs on safety work. It maintains a film library in connection with safety work and now has 23 films in its library available

without charge to anyone desiring to use such films on traffic safety. It has sponsored summer session courses at the University of California in driver education and driver training (R. 209-212).

Viewing all of the major activities of appellee as above outlined, as well as other activities referred to in testimony and in stipulated documentary evidence, it is obvious that all of these activities were designed and carried on for the purpose of contributing to the comfort, convenience, contentment, satisfaction, pleasure and recreation of appellee's members. Any legislative accomplishment which provides for the opening, extension or improvement of highways, or making driving conditions safer and less onerous for the owner of a pleasure car, contributes to the physical as well as mental wellbeing, pleasure and recreation of the member.

Likewise, it is clearly apparent that the numerous safety measures instituted and carried on by appellee directly aid and benefit its members by making motoring conditions less hazardous, thus importantly contributing to their comfort, ease of mind and safety.

It is interesting to note on page 12 of appellant's brief his admission that the members of appellee no doubt "find considerable satisfaction and comfort" in knowing that they will be towed to a garage if necessity requires, etc.

On page 13 of appellant's brief he admits that although "in an extremely remote way" the recreation of appellee's members is involved in its operations.

From the foregoing recital of activities and accomplishments it appears that appellee has kept fully abreast of the times and has enlarged and expanded its field of activities over the years since its organization to keep pace with constantly changing problems created by the ever-increasing density of automobile traffic, and particularly the greatly increased speed of automobiles with its attendant danger to both pedestrian and other vehicular traffic. Thus safety measures and education have played a prominent part in the program of appellee. Can it be doubted that successful efforts of such a nature contribute very materially to the enjoyment, contentment, well-being, satisfaction, and both physical and mental relaxation and recreation of appellee's members, for whose benefit such projects are undertaken? The fact that incidentally other automobilists and the general public are also benefited and educated does not detract in any sense from the pleasure and recreation of the members, rather it enhances the consequential benefits to them.

During 1943 and 1944, the opportunity for furnishing customary services to appellee's membership was to a considerable degree curtailed because of war-time restrictions, gasoline rationing, and the difficulty of obtaining both labor and materials for road signing and other work. In spite of that fact, appellee carried on its activities to the greatest extent possible, but also bent its energies to assist in war work within the scope of its field of endeavor, and furnished many services and benefits to persons connected with the prosecution of the war as well as to Federal Government Depart-

ments and Agencies, such as, for instance, the construction and erection of about 8,000 dimout signs. It furnished instruction in the training of drivers for the American Red Cross and the American Women's Volunteer Service.

It should be noted, that services benefiting persons, other than members of appellee, as well as services rendered to the Federal Government, the Red Cross, and other agencies during the war, were furnished without cost, so that there was no element of profit involved in the rendition of such services in 1943 and 1944, or in any other year.

In that connection, it should be pointed out that certain activities which would result in the receipt of very small amounts of income had been abandoned prior to the year 1943. For example, the finance department, described on page 5 of Exhibit 1-D, was abandoned about February, 1942. The rental of a frame building used as a garage and located on appellee's San Francisco property was abandoned in October, 1941. The appellee had also abandoned, prior to 1943, special memberships to hotels, garages and road service stations from which a small amount of income had theretofore been received and all advertising revenue from the publication of the monthly magazine "Motorland" had ceased late in 1941. Likewise, appellee had eliminated, prior to 1943, the very small amount of income received from sales of license plate frames.

The receipt of a small amount of incidental income is not, however, under the authority of a number of decided cases, sufficient to destroy the tax exempt status of clubs otherwise qualifying under Section 101(9) of the Internal Revenue Code. This has been held to be true even in some instances where the amounts of such income were quite large and were from sources entirely dissociated from the main purpose of the club. The Supreme Court of the United States in *Trinidad v. Sagrada Orden*, 263 U. S. 578, pointed out, in a case arising under a somewhat similar provision of law, that the statute says nothing about the *source* of the income but makes its *destination* the ultimate test of exemption. That principle of law has been cited and followed by a number of Federal courts in cases involving the application of Section 101(9) of the code. In his affidavit of October 5, 1941 (Exhibit 1-D), Mr. Watkins made the following statement:

“Disposition of Income: The entire income of the Association is used to carry out the purposes recited in its Articles of Incorporation and to render to its members the various services previously enumerated. No distribution of income has ever been made to members nor does any profit inure to the benefit of any individuals.”

The testimony and exhibits in this case show that such statement was also true in 1943 and 1944, although war services were rendered to Governmental and other agencies, but the rendition of such services

would clearly qualify under the phrase in Section 101(9), "other non-profitable purposes".

One of the outstanding cases in the Federal Courts dealing with the exact question of the tax exempt status of certain corporations under Section 101(9) and other similar sub-sections, is *Koon Kreek Klub v. Thomas, et al*, 106 Fed. (2d) 616, decided by the Fifth Circuit Court of Appeals. In that case the appellant was organized as a fishing and hunting club, maintaining a clubhouse, boats, and fishing and game preserves for the pleasure and amusement of its members, and it acquired a tract of land containing 6,777 acres, which completely surrounded a tract of 340 acres owned and occupied by one Thomas. It granted grazing privileges to Thomas for a consideration of \$500 per year, and for a certain period extended similar privileges to its manager for \$100 per year. Prior to the tax years before the Court, the club received income from dues which averaged \$12,500 per year. Oil was later discovered about seven miles from the club property and in 1934, one of the years under consideration, the club granted an oil lease on its entire property at a rate of \$4.00 per acre, with an annual renewal rental of \$1.00 per acre, reserving the usual royalties. The lease was not renewed, however, and the amount received, which exceeded \$25,000, was used to reduce or retire a mortgage which had been outstanding against the property since its acquisition by the club.

The Court found that the question of tax liability turned upon the interpretation of Section 101(9) of

the Revenue Act of 1934 (identical in 1943 and 1944), and held that whatever financial gain was realized from the grazing and leasing activities was incidental to and directed toward the accomplishment of the purpose upon which the income tax exemption was based.

The Court continued:

“The contention that the club did not operate exclusively for non-profitable purposes because of the leases of grazing rights is equally without foundation. In order to maintain its houses and preserves, it was required to raise funds from some source. That these funds might be derived from a use of the properties themselves, *not inconsistent with the purposes for which they were maintained, would not change the nature of the operation any more than an increase in dues charged to members. Indeed, if the club could be made self-sustaining by grazing fees, guest fees and other prerequisites, its operations being for the stated purposes, its exempt status would not be affected.* We need but to extend this principle to the acquisition of the preserves themselves to demonstrate that the granting of oil leases to obtain money with which to pay the mortgage debt did not change the character of the organization.

* * * * *

“We think the question is controlled by the decision in *Trinidad v. Sagrada Orden*, 263 U. S. 578, 44 S. Ct. 204, 68 L. Ed. 458, wherein the court points out that the statute says nothing about the source of the income, but makes its destination the ultimate test of exemption. The act here involved provides exemption for ‘clubs organized

and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder', while the statute before the Supreme Court provided exemption for corporations 'organized and operated exclusively for religious, charitable, scientific or educational purposes, no part of the net earnings of which inures to the benefit of any private stockholder or individual'. *The necessity of having money to carry on the enterprise, whether charitable or recreational, is present in both cases. Deriving funds from the properties owned to further either of these ends would be no more a departure in one case than in the other.*" (Italics supplied.)

Likewise, it was held in *The Goldsby King Memorial Hospital, a Corporation v. Commissioner*, CCH Dec. 14042 (M) that a corporation otherwise exempt is not deprived of exemption because it incidentally carries on a profitable activity in furtherance of its predominant charitable purpose.

See also *Anderson Country Club, Inc. v. Commissioner of Internal Revenue*, 2 T. C. 1238, *Santee Club v. White*, 87 Fed. (2) 5, *Town and Country Club v. Commissioner* (CCH Dec. 12924-A, December 30, 1942), *Roche's Beach, Inc. v. Commissioner of Internal Revenue*, 96 Fed. (2) 776, *Schofield v. Corpus Christi Golf and Country Club*, 127 Fed. (2) 452.

In the latter case, where the club had executed an oil lease on its property and received very substantial sums as royalties and bonus under the lease, the Court said:

“The statute expressly gives the exemption to clubs operated as this one was and as long as the exemption holds, all revenues of the club without regard to their source, are exempt from tax, *because under the statute it is the nature and character of the operations of the club and the use made of the revenues, and not their source, which determines the exemptions.* The judgment was right. It is affirmed.” (Italics supplied.)

In *Forest Lawn Memorial Park Association, Inc. v. Commissioner of Internal Revenue*, 45 B.T.A. 1091, the Board of Tax Appeals held the petitioner corporation, which operated a cemetery for non-profit purposes, exempt from taxation under Section 101(5) of the Revenue Acts of 1934 and 1936, which granted exemption to cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit, etc. In that case, in addition to the usual functions of a cemetery, the corporation sold flowers, booklets, postcards, brochures, etc., and wedding ceremonies were conducted in the two churches within the cemetery without charge except for services.

The Tax Court of the United States (formerly the Board of Tax Appeals) considered for the second time, involving later years, the Commissioner's repeated assertion that the petitioner was not entitled to exemption under the same statutory provisions, and the Court's decision was rendered in the second case in *Forest Lawn Memorial Park Association, Inc. v. Commissioner of Internal Revenue*, 5 T.C.M. 738. The

Government's claim in the second case was based on (1) the incidental activities of petitioner and the profitable operation of the corporation, and (2) the close connection between the corporation and the manager's family and holding company.

In granting exemption for the second time, the Tax Court said:

"In presenting his case upon the merits respondent is confronted at the outset with the difficult task of successfully distinguishing this case from our prior decision. His contentions in the two cases are from necessity much the same. * * *

* * * * *

"It is true that petitioner operated Forest Lawn at a profit, but it cannot be said that it was a cemetery company organized or operated for profit. On the contrary it was organized as a non-profit cemetery company and it has made no distribution of profits to its members. Its predominant purpose, as we said in our prior opinion was 'to operate and maintain a cemetery for the interment of the dead.' 45 B.T.A. 1091, 1100. *No additional fact is presented or change in charter or by-law urged to show that petitioner has changed its predominant purpose during the taxable years. We can find no new or different activities on the part of petitioner which might indicate a change in its predominant purpose. It is our opinion, therefore, that petitioner continued during the taxable years to be a non-profit cemetery company and that any profit resulting from its sales and services was incidental to its primary function of operating and maintaining a cemetery for the interment of the dead. * * **" (Italics supplied.)

The Commissioner of Internal Revenue has not appealed the foregoing decision.

At the top of page 7 of appellant's brief the word "similar" has been bracketed in the quotation from the statute, and the quotation has been followed by the parenthetical statement "Italics supplied". We wish to make it clear that the word "similar" does not appear in the statute itself but has also been supplied.

On pages 12 and 13 appellant argues that appellee was not organized and operated exclusively for pleasure or recreation and that the words of the statute "and other non-profitable purposes" do not, under the rule of *ejusdem generis*, enlarge the meaning of the preceding words of the statute. The interpretation for which appellant contends would make the phrase "and other non-profitable purposes" quite meaningless and would violate the well established rule that every word in a statute is to be given some meaning. The use of the conjunction "and" shows quite clearly that Congress did intend to expand the category of exempt clubs. If appellant's contention were to be conceded the statute might well have read "clubs organized and operated exclusively for pleasure and recreation, no part of the net earnings of which inures to the benefit of any private shareholder".

The rule of *ejusdem generis* is not of universal application but is only a rule of interpretation and is subject to qualification. One such qualification is that meaning must be given to the general words on the assumption that Congress intended them to mean

something more and in addition to the specific words. The rule clearly is not to be applied to the extent of making the general words meaningless. In this connection it is worthy of note that while Section 101 of the Internal Revenue Code includes 19 subsections, the one with which we are here concerned, (9) is the only one of the 19 where specific words are followed by the phrase "and other non-profitable purposes."

The introductory language in Section 101 states that "The following organizations shall be exempt from taxation under this chapter * * *." Thus we start out with a broad classification in the statute followed by an enumeration of 19 kinds of organizations to which exemption has been granted.

An examination of Section 101(12), for example, shows that Congress knows how to limit general words in tax exemption statutes when a limitation is intended. In that section the expression "or like associations" is the limiting language, and is, in essence, what the Government is asking the Court in this case to read into subsection (9). We believe that if Congress had intended such a limitation in subsection (9) it would have inserted one as it did in subsection (12).

Section 101(8) extends exemption to "Civic leagues or organizations not organized for profit, but operated exclusively for the promotion of social welfare * * *" and under this subsection the *Pickwick Electric Membership Corporation* has been held exempt in 158 Fed. (2d) 272, although that corporation obviously is not a civic league in any sense of the word but does qualify

as an organization not organized for profit and operated exclusively for the promotion of social welfare. This would indicate that the use of general language such as "organizations organized for profit" following more specific words such as "Civic leagues" is not to be strictly limited by the specific words.

Indeed, there is evidence that the Government itself considers the phrase "and other non-profitable purposes" as a general description of clubs to be granted exemption under subsection (9), as is evidenced by the ruling in G.C.M. 22116, 1940-2 C.B. 100, *infra*, in which the M Alumni Association was exempt from tax under Section 101(9), and in I.T. 2693, XII-1 C.B. 59, *infra*, where tax exemption was allowed a club incorporated for the purpose of making roads and trails in certain mountains, "to erect camps and shelter houses therein, to furnish maps and guide-books thereof, and in other ways to make these mountains play a larger part in the life of the people."

The Supreme Court of the United States had occasion to consider the rule of *ejusdem generis* and the limitations thereon in *Helvering, Commissioner of Internal Revenue v. Stockholms Enskilda Bank*, 293 U.S. 84, 79 L. Ed. 211, where it said:

"But it is said that the phrase in question must be restricted in accordance with the rule of *ejusdem generis*. The point is not without merit. The phrase reads 'interest on bonds, notes, or other interest-bearing obligations.' If the rule invoked be held controlling, it would follow that the general words 'other interest-bearing obliga-

tions' must be assimilated to the particular words 'notes and bonds,' and restricted to obligations of the same kind. But while the rule is a well-established and useful one, it is like other canons of statutory construction, only an aid to the ascertainment of the true meaning of the statute. It is neither final nor exclusive. To ascertain the meaning of the words of a statute, they may be submitted to the test of all appropriate canons of statutory construction, of which the rule of ejusdem generis is only one. If, upon a consideration of the context and the objects sought to be attained and of the act as a whole, it adequately appears that the general words were not used in the restricted sense suggested by the rule, we must give effect to the conclusion afforded by the wider view in order that the will of the legislature shall not fail."

In *State of Texas et al. v. United States et al.*, 6 F. Supp. 63, p. 65, the Court said:

"First of all, the rule ejusdem generis is a rule of construction only 'to be used as an aid in the ascertainment of the intention of the lawmakers, and not for the purpose of subverting such intention when ascertained.' *Mid-Northern Oil Co. v. Walker*, 268 U.S. 45, 49, 45 S. Ct. 440, 441, 69 L. Ed. 841."

Appellant, on page 13 of his brief, says that in interpreting a similar statute, referring to Section 101(9) of the Code, the Court in *Better Business Bureau v. United States*, 326 U.S. 279, held that the word "exclusive" in the statute meant just what it said and is not to be interpreted otherwise. We cannot

agree that the Court made any such holding in that case. The question there involved was whether the Better Business Bureau of Washington, D. C., was entitled to exemption from social security taxes as a corporation organized and operated exclusively for scientific or educational purposes within the meaning of Section 811(b)(8) of the Social Security Act. In the course of its discussion the Court made the following statement:

“In this instance, in order to fall within the claimed exemption, an organization must be devoted to educational purposes exclusively. This plainly means that the presence of a single non-educational purpose, *if substantial in nature*, will destroy the exemption regardless of the number or importance of truly educational purposes.” (Italics supplied.)

The above modification “if substantial in nature” does not accord with appellant’s interpretation as set forth in his brief but, on the contrary, is in accord with the earlier holding of the Supreme Court in *Trinidad v. Sagrada Orden*, *infra*, which likewise permitted departure from a strict and literal construction of the term “exclusive”, and has been cited by many Courts to emphasize such departure. A few such decisions have already herein been discussed or cited. The *Sagrada Orden* case dealt with a statute exempting corporations from income tax if organized and operated “exclusively” for religious, charitable, scientific or educational purposes, no part of whose net income inures to the benefit of any individual.

The qualifying phrase above referred to in the *Better Business Bureau* decision "if substantial in nature" is, of course, of the utmost importance and permits a taxpayer to engage, to a limited extent, in activities beyond the strict scope of the purposes enumerated in such tax-exempting provisions as Section 101(6), considered in the *Better Business Bureau* case, and Section 101(9) here involved.

On page 14 of his brief, appellant contends that a golf, rod or gun club may be income tax exempt under the section here involved, but the automobile club is a different type of organization and believes that most anyone, "including members of Congress", would think so. Assuming, *arguendo*, that may be so, it by no means follows that both types of clubs may not be tax exempt under Section 101(9). There is no language in Section 101(9) which limits exemption to golf, rod, gun and similar clubs, nor, indeed, has the Bureau of Internal Revenue itself limited such exemption to the type of club described by appellant. See, for example, G.C.M. 22116 and I.T. 2693, *infra*.

Appellant also, on page 14, states that this case is quite obviously important from a revenue standpoint. We respectfully submit that its asserted importance from such a standpoint is no reason for denying tax exemption, and we are confident that the Court will consider and decide this case only upon its merits. Also, if the Government means that an affirmation by this Court of the judgment of the lower Court means that the overall revenues of the Government will be seriously affected, we believe such a contention to be

wholly untenable, in view of the vast tax revenue collected by the Government each year as compared with the very limited number of automobile clubs throughout the United States, and their insignificant effect upon the revenues, even if all of them were able to qualify for exemption under Section 101(9).

D. NO PART OF THE NET EARNINGS OF APPELLEE HAS EVER INURED TO THE BENEFIT OF ANY PRIVATE SHAREHOLDER OR MEMBER.

No stock has ever been issued to members of appellee and it has never paid dividends of any nature to any member. None of its income has ever been paid or credited to any member on its books, no provisions have ever been made to pay or to credit any net earnings to its members, nor has appellee any plan or purpose to distribute its net earnings so as to inure to the benefit of any individual member. Further, no director of appellee nor any officer, as such, received any salary or other compensation in 1943 or 1944.

The amendment of Article VI of the original Articles of Incorporation points out (Exhibit 1-B):

“That said Corporation is not organized for pecuniary profit * * *.”

As previously stated, the entire income of the appellee is normally used to carry out the purposes for which it was incorporated and to render to its members the various services hereinbefore outlined. The amounts so expended were, however, below normal in

1943 and 1944 as in those years appellee was rendering services connected with the war effort, and in addition had to economize on both labor and materials, both of which were difficult to obtain, so that wartime restrictions, as found by the Court below, prevented it from expending all its annual receipts in 1943 and 1944.

In *Koon Kreek Klub v. Thomas, et al.*, *infra*, the Court said that so long as profits “are retained by the organization or used to further the purposes which are made the basis of exemption and are not otherwise used for the benefit of any private shareholder * * *,” such profit cannot be deemed to inure to the benefit of any private shareholder.

Appellee’s Exhibit 4, entitled “Composition of Surplus Balance”, covers the period annually from December 31, 1931 to December 31, 1946, together with the first quarter of 1947, representing an analysis of appellee’s surplus account taken from its records. This statement, in the third column, shows the amount of the unexpended income after taking out the amount of unearned dues for each year beginning December 31, 1937, down to and including March 31, 1947. That column shows an excess of \$7,868.71 at December 31, 1937, which changed into a deficiency in 1938 and continued in 1939 and 1940. During the next five years, the income exceeded the expenses and as a result there was a surplus balance for those years. In 1946, the expenditures exceeded the income, resulting again in a deficiency, and there was also a deficiency for the first quarter of 1947.

The fifth column shows that for the sixteen years included in said statement, eight years were in the black and eight years in the red. Consequently, in some years appellee took in more than it spent, and in others spent more than it received during the year.

We believe it is clear that no part of appellee's net earnings has inured to the benefit of any member, and that it was never intended that they should.

E. DUE REGARD MUST BE GIVEN TO THE OPPORTUNITY OF THE TRIAL COURT TO JUDGE THE CREDIBILITY OF THE WITNESSES AND TO VIEW THE EVIDENCE.

The only evidence adduced in the Court below was the oral testimony of witnesses offered by appellee together with documentary evidence. No witnesses were offered on behalf of appellant.

Rule (52(a) of the Rules of Civil Procedure for the District Courts of the United States provides in part:

“Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses.”

In *Wittmayer v. United States*, 118 Fed. (2d) 808, 311 (C.C.A. 9th), this Court stated in interpreting Rule 52(a) that:

“The provisions of the new procedural rules that the findings of fact of the trial judge are to be accepted on appeal unless clearly wrong (Rule 52(a), 28 U.S.C.A. following Section 723c), is but the formulation of a rule long recognized and ap-

plied by courts of equity. *Guilford Const. Co. v. Biggs*, 4 Cir., 102 F. (2d) 46, 47.

“As was said by Mr. Justice Holmes in *Adamson v. Gilliland*, 242 U.S. 350, 353, 37 S. Ct. 169, 170, 61 L. Ed. 356 (citing *Davis v. Schwartz*, 155 U.S. 631, 636, 15 S. Ct. 237, 39 L. Ed. 289), the case is pre-eminently one for the application of the practical rule, that so far as the findings of the trial judge who saw the witnesses ‘depends upon conflicting testimony or upon the credibility of witnesses, or so far as there is any testimony consistent with the finding, it must be treated as unassailable.’ ”

Similarly, in *United States v. Aluminum Co. of America*, 148 F. (2d) 416, 433, the Court of Appeals for the Second Circuit held that when a trial judge has seen the witnesses:

“* * * and in so far as his findings depend upon whether they spoke the truth, the accepted rule is that they ‘must be treated as unassailable.’ *Davis v. Schwartz*, 155 U.S. 631, 636, 15 S. Ct. 237, 39 L. Ed. 289; *Adamson v. Gilliland*, 242 U.S. 350, 353, 37 S. Ct. 169, 61 L. Ed. 356; *Alabama Power Co. v. Ickes*, 302 U.S. 464, 477, 58 S. Ct. 300, 82 L. Ed. 374. * * *; and upon an issue like the witness’s own intent, as to which he alone can testify, the finding is indeed ‘unassailable,’ except in the most exceptional cases.”

In the light of the foregoing interpretations by this Court, as well as by the Second Circuit Court of Appeals, in the cases cited, attention is again invited to the findings of the lower Court in the case at bar, particularly the following:

“That the sum total of the activities of the Plaintiff is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by Plaintiff are for the pleasure and recreation of its members (R. 84).”

“That none of the normal activities or the wartime activities of the Plaintiff were conducted for the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities (R. 84-85).”

“It has been the policy of the Plaintiff to expend on services all its annual receipts, and during 1943 and 1944 it was prevented from so doing only by reason of wartime restrictions. That in the 16-year period from and including 1931 to 1946 the Plaintiff has had a deficit in 8 years and a surplus in 8 other years (R. 85).”

“That the Plaintiff has never distributed, set aside, or credited on its books by way of dividends or from its earnings any money to any of its members as an incident of their membership in the Plaintiff association. That there has never been any intention to distribute any net income direct to the members. That the directors of Plaintiff serve without financial remuneration (R. 85).”

“That the Plaintiff has only the powers necessary to carry out its purposes. The Plaintiff has no power to distribute or set aside any portion of its net income to its members or to any other person except to carry out its purposes (R. 83).”

“That the Plaintiff is a continuing organization whose members make common cause both in

a financial sense and in carrying out its stated purposes by group activity as well as by individual action (R. 85).’’

“That Plaintiff association is a club (R. 86).’”

Consequently we believe that the foregoing findings, together with other findings of the trial Court, conclusively show that appellee fully meets the requirements of Section 101(9) of the Internal Revenue Code, and that such findings, in the language of *Wittmayer v. United States, supra*, must in the language of this Court, “be treated as unassailable”.

CONCLUSION.

The judgment of the District Court was correct and should be affirmed.

Dated, San Francisco, California,
January 26, 1949.

Respectfully submitted,

ARTHUR H. DEIBERT,

GEORGE E. SANDFORD,

Attorneys for Appellee.

No. 12,055

IN THE

United States Court of Appeals
For the Ninth Circuit

JAMES G. SMYTH, Collector of Internal
Revenue of the First Internal Revenue
Collection District of California,

Appellant,

VS.

CALIFORNIA STATE AUTOMOBILE ASSOCIA-
TION, a corporation,

Appellee.

APPELLEE'S PETITION FOR A REHEARING.

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(FILE)

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PAUL P. O'BRIEN

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APPELLEE'S PETITION FOR A REHEARING.

*To the Honorable William Denman, Chief Judge, and
to the Honorable Associate Judges of the United
States Court of Appeals for the Ninth Circuit:*

Appellee respectfully petitions the Court for a rehearing of the above-entitled cause in the light of the Court's opinion filed herein on June 22, 1949, based upon the following grounds:

1. That Article III of the By-laws of Appellee (hereinafter called the Association) relating to membership, as set forth in the opinion of the Court on pages 2 and 3 thereof, are the same as they were from

the date of the adoption of the first By-laws of the Association on September 14, 1907, to the present time, with the exception that Section 1 of Article III of the original By-laws contained the word "male" so that they read: "All male persons interested in the objects of this Association as hereinabove set forth shall be eligible to membership", and that the word "male" was deleted therefrom by an amendment adopted October 6, 1915, since which date there has been no change in said Section 1 or Section 2 of Article III of the Association's By-laws; that in spite of such provision as to membership, the Commissioner of Internal Revenue allowed exemption from income tax to the Association from 1913 to 1943.

If the Court deems it necessary to establish the facts with reference to the provisions of the Association's By-laws from 1907 to and including the year 1944 relating to Membership and Purposes and Powers, we respectfully request that the case be remanded to the trial Court for the purpose of receiving whatever testimony and documentary evidence may be necessary to establish such facts.

2. That the amendment of Article II of the Articles of Incorporation of the Association in 1929 was not considered by the Commissioner of Internal Revenue as a reason for denying further exemption to the Association beginning January 1, 1943, but that such exemption was denied for reasons which make no reference to the said amendment of Article II in 1929.

3. That the Association should not be deprived of its exemption from taxation, which existed for thirty

years from 1913 to 1943, for the reason that because of shortage of labor and materials and restrictions on use of automobiles during 1943 and 1944, it voluntarily devoted a portion of its resources and efforts to rendering patriotic services in furtherance of the war effort.

4. That the Association did not issue special memberships to hotels, garages and road service stations in 1943 or 1944, and as those were the only two years before the Court, it is respectfully urged that the issuance of such memberships in earlier years has no bearing upon and is not material in determining the tax exempt status of the Association for 1943 and 1944, the only years before the Court.

5. The Association further respectfully urges that in view of the fact that the Court's opinion of June 22, 1949, is based primarily upon issues not argued either on brief or orally before either this Court or the trial Court, the Association should now be granted the privilege of a rehearing so that it may have the opportunity of presenting authorities and arguments upon such issues.

ARGUMENT IN SUPPORT OF GROUNDS FOR REHEARING.

Grounds 1 and 2.

Grounds 1 and 2 will be discussed together in view of their close relationship. The first ground for reversal stated in the Court's opinion deals with its statement that the Association was organized to serve commercial as well as pleasure vehicles, and consider-

able stress is laid upon the amendment of Article II of the Articles of Incorporation of the Association in 1929, as set forth on page 2 of the Court's opinion.

There is a number of cases in which the form of organization of the corporation, the statutes under which it was organized, and powers outlined in the charter, have been held not decisive of the question as to whether it was actually "organized" for such purposes.

In *Koon Kreek Klub v. Thomas*, 108 Fed. (2d) 616, the Fifth Circuit Court of Appeals did not deny exemption under Section 101 (9) of the Internal Revenue Code, in spite of the fact that the club was authorized to raise livestock for profit. The Koon Kreek Klub was organized primarily as a fishing and hunting club maintaining a club house, boats, and fishing and game preserves for the pleasure and amusement of its members and it acquired a tract of land containing 6,777 acres, which completely surrounded a tract of 340 acres owned and occupied by one Thomas. It granted grazing privileges to Thomas for a consideration of \$500 per year, and after oil was discovered about seven miles from the club property the club granted an oil lease on its entire property for \$4 per acre, with renewal privileges, reserving the usual royalties. The club received from its lease an amount of \$24,000 in 1934.

With respect to raising livestock for profit, which was clearly not in itself an activity relating to pleasure and recreation, the Court said:

“The provision of the charter authorizing the club to engage in the business of raising live stock for profit, having been brought about by the prosecution of the original purpose of the club, and having been exercised to that end alone, does not change the character of the corporate entity from one clearly exempt, under the terms of the act, to one outside the exemption provisions. The express grant of authority must be construed in the light of the admitted purpose and operation of the club and its needs to accomplish its ends, and not abstractly to draw it within the terms of the statute, without regard to its purposes and intentions as a matter of fact. * * *”

In *Commissioner v. Battle Creek, Inc.*, 126 F. (2d) 405, the corporation was organized under the general corporation laws and was authorized to conduct “any lawful business”. The corporation was not denied exemption simply because it was so organized. The Court said:

“It is not unusual for charters or corporations to grant broad powers and privileges that are never intended to be used”.

It is believed the Court will take judicial notice of the fact that many corporations are so organized.

In *Anderson Country Club v. Commissioner*, 2 T.C. 1238, exemption was allowed even though the Club was organized under the general corporation law, and also gave the specific power to, and expressed as one of its objects, the buying, selling and leasing of real estate, normally an activity conducted for profit.

In *Sands Springs Home*, 6 B.T.A. 198, the corporation was given extremely broad powers to conduct business and did, in fact, conduct a power, light and water company, a gas company, a greenhouse, a cotton gin, an amusement park operated for profit, and other businesses. It was, nevertheless, held tax exempt under Section 231 (6) of the Revenue Act of 1921, as a corporation "organized and operated exclusively" for charitable purposes, no part of the net earnings of which inured to the benefit of any private stockholders or individual.

In *Roche's Beach, Inc. v. Commissioner*, 96 F. (2d) 776, the corporation was organized under the general corporation laws and was authorized to do business. There were no restrictions on its use of income. It was, nevertheless, held exempt as a charity where all the proceeds were, in fact, turned over to an exempt charity. Evidence outside of the charter was admitted to show the purposes of its organization. The Bureau recognized the rule of the *Roche's Beach* case for some time, but then withdrew its recognition. However, the Tax Court in *Estate of Louise V. Simpson*, 2 T.C. 693, has specifically indicated that it still accepts the *Roche's Beach* rule in spite of the Bureau's rejection of it.

In *Unity School of Christianity v. Commissioner*, 4 B.T.A. 61 (acq.) the corporation was organized under the general corporation law and its purposes and authority were broad to enable it to engage in any business. It was, nevertheless, held exempt, the Board of Tax Appeals stating that a corporation otherwise

exempt from tax is not deprived of exemption because it carries on profitable or competitive activities in furtherance of its predominant religious, charitable, scientific, or educational purposes.

In *Goldsby King Memorial Hospital*, 3 T.C.M. 693, the Court did not refuse exemption where the articles were broad enough to encompass a profitable business and it was organized under the general corporation law. There was in this case, however, as in ours, a provision against any portion of the profits inuring to the benefit of a private individual.

In *I. T. 1914*, III-1, Cumulative Bulletin, Bureau of Internal Revenue, 287, a corporation was held exempt as a farmers cooperative under the 1918 Revenue Act even though its articles gave broad powers to engage in business for profit. It was ruled that the actual conduct governed rather than the stated purpose.

In *I. T. 2325*, V-2 C.B. 63, an agricultural fair association did not lose exemption because its certificate of incorporation gave it broad powers, since its actual activities were confined to exempt activities.

In *A.R.R. 218*, III C.B. 238, a teachers' insurance and annuity association whose purpose was to provide insurance and annuities to teachers on a *non-mutual, non-participating* basis was held exempt. The ruling said that under Solicitor's Opinion 20, the term "organized" as used in Section 231 (6) of the Revenue Act of 1918, refers to the real substance and intent of the organization and not to its mere form, the charter and by-laws merely giving rise to presump-

tions which may be affirmed or rebutted by extraneous evidence.

All of these cases and rulings stated for the principle that the expressed purpose is not necessarily determinative, and they are also indicative of the fact that it is not material that the type of business carried on is one usually conducted for profit, e.g., the operation of a bathing beach, insurance agencies or insurance company, raising of livestock, etc.

In its opinion, this Court also refers to the fact that at the time of the amendment of Article II of the Articles of Incorporation in 1929, many passenger cars were used by commercial agents in the course of their business and many more were used by persons going to and from their places of business, so that by 1943 and 1944 the Association's facilities were used to some extent for purposes other than pleasure and recreation. It is respectfully urged that this is not the criterion by which to decide the question of the Association's exemption under Section 101 (9) of the Internal Revenue Code, since the purpose of the Association is not to be determined by the use to which it is put by its members. It would be entirely erroneous, we believe, to deny tax exemption to a luncheon club or a golf club simply because some of the members of such clubs use the club facilities as a means of making and continuing business and professional contacts which are intended to and actually do serve the business and professional, rather than the pleasure and recreation, interests of such members. Such a practice is now and has been for many years so wide-

spread and so well known that it is believed the Court will take judicial notice of the practice. In fact, in some cases the making of business contacts or furthering business or professional interests is the sole or practically the sole reason for taking out such memberships, and in *Johnson v. United States*, 45 Fed. Supp. 377, decided by the District Court for the Southern Division of California, dues paid to two Country Clubs were held to be deductible as business expenses of two members who paid such dues for the purpose of obtaining business.

In addition, we believe that the Treasury Department was fully cognizant in 1929, when the amendment quoted by the Court was made to the Association's Articles of Incorporation, that passenger cars might be put to commercial use and were so being used. The Court has taken judicial notice of such fact and it would seem that the Treasury might also be charged with such notice. In any event, as will later be pointed out, it was the policy of the Government at that date to allow exemption of automobile clubs generally, in spite of the fact that obviously there must have been wide variations and occasional changes both in Articles of Incorporation and By-laws of such clubs.

In *O.D. 340*, I C.B. 202, an organization incorporated for the purpose of maintaining a day nursery for the children of working parents, and supported by donations, was held exempt. It would seem clear in this case that the parents were using the facilities to further their business interests and yet the nursery itself was not denied exemption.

In *I.T. 2296*, V-2 C.B. 65, a club whose object was encouragement of artistic handcraft work sold articles for its members and for *non-members* and charged a commission for the sale. It would seem clear that the club was participating in a business normally carried on for profit, and was being used by its members and outsiders as a means for accomplishing sales of their products. Such a use by the members and non-members did not defeat the club's exemption.

Similarly, in *S.M. 5516*, V-1 C.B. 81, an exchange incorporated for the purpose of giving employment to deserving women was held exempt. It was supported by donations and commissions on sales of handcraft articles. Clearly this organization was being used to further the commercial interests of its members.

In *Pasadena Methodist Foundation*, 2 T.C.M. 905, exemption was not refused a religious corporation even though it served as trustee of three trusts, administering them for the benefit of the donors who retained a life estate. The donor clearly was using the trustee's services to further its individual interests, and the individual's purpose did not defeat the exemption of the organization.

In a similar case, *Orton Ceramics Foundation v. Commissioner*, 9 T.C. 533, exemption was not refused a scientific foundation simply because it was operated partly for the purpose of providing a life annuity to the founder's widow.

Exhibit 1-D in the present case is the affidavit of D. E. Watkins, Secretary of the Association, executed

on October 5, 1941, which was prepared and forwarded to the Bureau of Internal Revenue at the request of the Collector of Internal Revenue at San Francisco in response to the latter's request dated September 10, 1941, Exhibit 1-C. One of the enclosures with Mr. Watkins' said affidavit forwarded to the said Collector by the Association in October, 1941, was Exhibit 1-B, which contains, *inter alia*, the amendment of Article II of the Articles of Incorporation of the Association adopted by the Board of Directors on August 8, 1929, and from which the Court quotes on page 2 of its opinion. The Commissioner of Internal Revenue consequently had before him on September 23, 1944, the date of his first letter denying further exemption to the Association, beginning January 1, 1943, the said amended Article II. In fact, in the second paragraph of the first page of said letter of September 23, 1944 (Exhibit 1-E), the Commissioner specifically refers to the provisions of that amended Article in the following language: "To furnish advice, information and assistance to owners and operators of self-propelled vehicles * * *". The Commissioner also took cognizance of the provisions of the Association's By-laws in the following language in paragraph 3 of the first page of the aforesaid letter, in which he states:

"Your By-laws provide that all persons and associations similar to yours which are interested in the objects of your Association shall be eligible to membership * * *".

In spite of these facts, the Commissioner did not use either the quoted provisions of the By-laws or the

aforesaid amendment of Article II as a basis for his ruling denying tax exemption. Rather, the Commissioner predicated his ruling in large part upon the decision in *Arner v. Rogan* (May 20, 1940, C.C.H. par. 9567) and held that the organization there under consideration was not a club because there was no comingling of members or fellowship among members. The Commissioner further in the said letter stated that the Association's principal activity was that of rendering services to members of the type available to motorists generally on a commercial scale at greater cost. It is believed that the record completely refutes such assertion.

As the record further shows, the Association protested the aforesaid ruling of September 23, 1944, and upon reconsideration the Commissioner of Internal Revenue on July 27, 1945, sent a letter (Exhibit 1-G) to the Association and confirmed the adverse ruling of September 23, 1944, *supra*, stating that in G.C.M. 23688 (C.B. 1943, 283) it was concluded for the reasons therein stated that the M Automobile Association was not entitled to tax exemption under Section 101 (9) of the Code; that this opinion was first published during the first part of July, 1943, and in the light of the view expressed in G.C.M. 23688, it was concluded that the Association at bar was not entitled to tax exemption under Section 101 (9). We have heretofore commented at length in our brief in this Court upon the inapplicability of G.C.M. 23688 to our case.

In connection with the aforesaid letter of July 27, 1945, it is pertinent to note the statement by the Commissioner of Internal Revenue that "Prior to the time that the information submitted by you in 1941 was taken up for consideration a substantial number of automobile clubs had been held to be entitled to exemption under Section 101 (9) of the Internal Revenue Code and prior Revenue Acts".

At the trial of the present case in the District Court, the Government was represented by an assistant United States Attorney at San Francisco, who stated (Tr. 106-107) "In connection with the failure of the Commissioner to act promptly after 1941, I take it, is explained by the fact that *this action was a national action taken as to all similar clubs in 1943* and had not been taken as to any of them prior to that time. There is no difference between 1941 and 1943, as far as this club is concerned, or any other club in the United States. That followed G.C.M. 23668, which was issued in 1943. In other words, *it was a change at that time of the Department in reference to all clubs*". (Italics supplied.)

There seems to be no doubt that the action with reference to at least a large number of automobile clubs in the United States, denying them further exemption, was taken by the Commissioner of Internal Revenue in or about 1943, as part of a general policy, and that prior thereto tax exemption had been very generally accorded automobile clubs for many years. It is quite obvious that such clubs did not have identical articles of incorporation or by-laws, but that such

exemption had been very generally granted by the Commissioner of Internal Revenue over a long period of time without regard to specific provisions as to purposes and membership, which must have varied widely. In this connection it is quite significant that the Commissioner of Internal Revenue, even after receiving the general information contained in Mr. Watkins' affidavit of October 5, 1941 (Exhibit 1-D), including reference to the amendment of Article II of the Articles of Incorporation in 1929, and being advised also as to the qualifications for membership, both as outlined in the aforesaid letter of September 23, 1944 (Exhibit 1-E), did not base his adverse ruling upon either the aforesaid amendment of Article II of the Articles of Incorporation or of the provisions of the By-laws relating to membership.

The significance of the foregoing lies in the fact that exemption prior to 1943 had been given to automobile clubs, including ours, without regard to the lack of social features, and without limiting the operation of the statute in certain cases to strict pleasure and recreation purposes. (See Bureau rulings cited on pages 25 and 26 of our brief.) Instead, the Treasury Department had allowed such clubs exemption, obviously interpreting the words "and other non-profitable purposes" to mean something different from strict pleasure and recreation. The exempting statute was repassed repeatedly while this interpretation was in effect. This is significant for two reasons—first, it indicates that the denial of exemption in our case was part of a general change in interpretation rather than

due to any act of the Association itself confirmed by the statement of Government Counsel in the trial Court hereinabove quoted (Tr. 106-107) that "this action was a national action taken as to all similar clubs in 1943" and that "it was a change at that time of the Department in reference to all clubs;" and, second, such changed administrative interpretation was improper because of the repeated reenactment of the exempting law.

In the Association's brief in this Court, we cited on page 33 the decision of this Court in *Bryant v. Commissioner*, 111 Fed. (2d) 9, in which the Court said:

"The established administrative practice of so many years, during which time the exemption was several times reenacted, carries weight as a construction of the statute which is not offset, at least as to the tax year in question, by the later expression of opinion in G.C.M. 16861, XV-2 Cum. Bull. 179 (1936)".

The principle thus stated is well established. See also the decision of this Court in *Citizens National Trust & Savings Bank of Los Angeles v. United States*, 135 Fed. (2d) 527, on pages 33 and 34 of our brief.

The Supreme Court of the United States in *Helvering v. Bliss*, 293 U.S. 144, 79 L.Ed. 246, stated in connection with the right to a deduction on account of charitable contributions:

"If the meaning of the Act were doubtful, we should still reach the same conclusion. The ex-

emption of income devoted to charity and the reduction of the rate of tax on capital gains were liberalizations of the law in the taxpayer's favor, were begotten from motives of public policy, and *are not to be narrowly construed.* * * * Moreover, from 1923 to 1932 the Commissioner uniformly ruled that the deduction for charitable contributions was to be taken from net income before computation of the tax and hence in whole from ordinary net income. *The reenactment in later Acts of the sections permitting the deduction indicates Congressional approval of this administrative interpretation.*" (Italics supplied.)

The Supreme Court of the United States again spoke on this question in *Helvering v. R. J. Reynolds Tobacco Co.*, 306 U.S. 110, 59 S.Ct. 423. In that case the Commissioner's regulations, in effect in 1929, provided that:

"A corporation realizes no gain or loss from the purchase or sale of its own stock"

and they had so provided since 1920. The Court there said:

"The administrative construction embodied in the regulation has, since at least 1920, been uniform with respect to each of the revenue acts from that of 1913 to that of 1932, as evidenced by Treasury rulings and regulations, and decisions of the Board of Tax Appeals. In the meantime successive revenue acts have reenacted, without alteration, the definition of gross income as it stood in the Acts of 1913, 1916, and 1918. Under the established rule Congress must be taken to have approved the administrative construction and thereby to have given it the force of law."

See also *Helvering v. Griffiths*, 318 U.S. 371, 63 S. Ct. 636.

As stated on page 10 of our brief, the exempting provision in question in our case has been enacted by Congress eleven times.

The record in this case shows (see pages 8-11, 31-33 of our brief in this Court) that there had been practically no change in the wording of what is now Section 101 (9) of the Code from 1916 down to the present, and that so far as the regulations issued under Section 101 (9) of the Code and similar sections under the prior Revenue Laws beginning with 1916 are concerned there had been no substantial change for a number of years except to more specifically define tax exempt clubs and to broaden the category of such clubs to include those meeting the description set forth in Regulations 111 (19.101 (9)) : "Generally, an incidental sale of property will not deprive the club of the exemption".

Ground 3.

The Association feels strongly that its patriotic endeavors to furnish services in furtherance of the war effort to the extent of its abilities during the years before the Court, 1943 and 1944, should not be used as a means of depriving it of its prior thirty years of tax exemption, but that the rendition of such services should be treated as arising out of the emergencies of war, which we request the Court to judicially notice as not an event normally taken into consideration by legislative bodies in the enactment

of legislation during periods when the country is not engaged in war. The record in this case shows that the Association spent considerable time, money and effort in furthering the cause of the United States in the Second World War, and we believe its right to tax exemption should not be denied because of the absence of legislation specifically authorizing it to render such services, but that the situation existing in 1943 and 1944 should be treated as an emergency challenging citizens acting either individually or in corporate form to render such services as they could in support of their country's cause without being penalized for so doing.

In addition, we believe the Court's reasoning gives no effect to the words of Section 101 (9) "and other non-profitable purposes". It is, of course, a cardinal principle of construction that effect must be given, if possible, to every word and phrase in a statute. The phrase "pleasure and recreation" is clear and unambiguous, and it is difficult to conceive of additional "non-profitable purposes" so like pleasure and recreation as to require the application of the doctrine of *ejusdem generis*. On the contrary, we believe that "other non-profitable purposes" was clearly intended to enlarge the field of purposes which would still entitle a club to exemption, even though not found within the well understood meaning of "pleasure and recreation * * * purposes", and that the war services rendered by the Association should be held to fall within the category of "other non-profitable purposes". Otherwise it would seem that the Court's reasoning

could be used to defeat the exemption of every other type of non-profit or charitable corporation which engaged in volunteer war work.

Further, we do not believe the Association is properly subject to criticism for exercising its right to test administratively and in the Courts the legality of a tax imposition merely because certain war years are involved, and particularly where, as in the case at bar, the Association had been granted tax exemption as shown by the record for thirty years, from 1913 to 1943. In fact, it is a matter of common knowledge that the Bureau of Internal Revenue and the Courts as well have been considering, and will for a number of years to come, questions as to the legality of taxes imposed by the Commissioner of Internal Revenue during the period of the Second World War. As an illustration, Section 722 and other sections of the Internal Revenue Code were enacted expressly by Congress to afford relief under specified circumstances to taxpayers who paid large excess profits taxes during the war years, and where because such special circumstances existed Congress has said that such taxes should not have been imposed.

The Association must likewise respectfully dissent from the Court's conclusion, stated on pages 4 and 5 of its Opinion in this case, that, because of the Association's contention as stated, *any* association of automobile users, if not yielding a profit to its members, is a "club" within Section 101 (9), and that it would cover a non-profit association solely to serve commercial agents using automobiles in carrying on their

business in California, or to serve the hotels, garages and service stations actually served in prior years. We believe that such a result could not ensue for the reason that the provisions of Section 101 (9) with reference to pleasure and recreation might be ignored in such instances and, therefore, be ineligible for exemption under Section 101 (9).

Ground 4.

We believe that the point made by the Court in the first paragraph on page 6 of its Opinion has no application to this case, in view of the fact that special memberships to hotels, garages and service stations had been abandoned prior to 1943, so that such memberships were not issued and are not involved in the two years before the Court, 1943 and 1944. That fact, together with the elimination of other small amounts of income, was pointed out in the last paragraph on page 44 of the Association's brief reading as follows:

“In that connection, it should be pointed out that certain activities which would result in the receipt of very small amounts of income had been abandoned prior to the year 1943. For example, the finance department, described on page 5 of Exhibit 1-D, was abandoned about February, 1942. The rental of a frame building used as a garage and located on appellee's San Francisco property was abandoned in October, 1941. The appellee had also abandoned, prior to 1943, special memberships to hotels, garages and road service stations from which a small amount of income had therefore been received and all advertising revenue from the publication of the monthly magazine

‘Motorland’ had ceased late in 1941. Likewise, appellee had eliminated, prior to 1943, the very small amount of income received from sales of license plate frames.’

Although we believe that the fact the Association had no such special memberships in 1943 and 1944 disposes of that issue, we feel the Court is in error in its statement that the Association’s brief admits that such special memberships “contributed to its income for its services to them”. The paragraph just above quoted, we respectfully submit, does not make such an admission. On the contrary, the Association intended to benefit its members and add to their pleasure and recreation by advising them of hotels, garages, etc., investigated and approved by the Association within the latter’s territory, so that its members when traveling would have lists of such approved hotels, garages, etc., might know the class of service to be there obtained, their locations, rates, and comparative ratings, all of which would contribute to their satisfaction and comfort and eliminate worry as to where they might safely stay or obtain other needed services while on pleasure trips particularly. Nor do we agree that the income referred to by the Court was used for a service other than exclusively for the pleasure and recreation provided in the exemption. The income from such special memberships was placed in the general funds of the Association which, we contend, were used for services exclusively for the pleasure and recreation of the members.

The Court then distinguishes from the present case the cases of *Koon Kreek Klub v. Thomas*, 108 Fed. (2d) 616, and *Trinidad v. Sagrada Orden*, 263 U.S. 578. The latter case will serve to illustrate, we believe, that there is no difference between the cases cited and the case at bar on the point made by this Court that "Here prior to 1943 the income from all sources, including the hotels, garages and service stations, was used in part to serve their commercial purposes". As we interpret the Court's language its meaning is that the income from the special memberships in question was used together with income from other sources in part to increase the business and profits of the hotels, garages and service stations. That, of course, was not at all the purpose of the Association, as above stated, which was to perform a service to its members in furnishing them with lists of approved hotels, etc. If such purposes of the Association resulted in incidental profit to the hotels, garages and service stations, the same identical result occurred in the *Sagrada Orden* case where some of its income came from " * * * sums received, in excess of cost, for wine, chocolate, and other articles *purchased* and supplied for use in its churches, missions, parsonages, schools, and other subordinate agencies". Such purchases, while made for the benefit of the corporation and to further its purposes, had the effect of increasing the sales and consequent profits of the persons who sold such articles to the corporation.

As above set forth, however, we believe these special memberships should play no part in a determination

of the Association's tax-exempt status in 1943 and 1944, the only years before the Court, inasmuch as there were no such memberships in those years.

Ground 5.

We respectfully request the Court to grant this Petition for Rehearing upon the further ground that what appear to be the basic reasons for the Court's opinion were not argued either on brief or orally before the trial Court or this Court, so that we may have the opportunity of presenting authorities and arguments upon such issues.

Dated, San Francisco, California,

July 22, 1949.

ARTHUR H. DEIBERT,

GEORGE E. SANDFORD,

Attorneys for Appellee

and Petitioner.



CERTIFICATE OF COUNSEL.

In the judgment of the undersigned Attorneys for Appellee, this Petition for Rehearing is well founded, and it is not interposed for delay.

Dated, San Francisco, California,
July 22, 1949.

Respectfully submitted,

ARTHUR H. DEIBERT,

GEORGE E. SANDFORD,

*Attorneys for Appellee
and Petitioner.*



No. 12056

United States
Court of Appeals

for the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA L.
BOULTER.

Appellants.

VS.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation.

Appellee.

Transcript of Record

FILED
DEC 15 1948

Appeal from the United States District Court
for the Northern District of California,
Southern Division

No. 12056

United States
Court of Appeals
for the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Appellants,

vs.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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In the Superior Court of the State of California,
in and for the City and County of
San Francisco

(District Court No. 27857 R—Civil)

No. 371020

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Plaintiffs,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant.

COMPLAINT

FIRST CAUSE OF ACTION

Comes now the plaintiff, George W. Boulter, and
complaining of the defendant alleges:

I.

That at all times herein mentioned the defendant, Commercial Standard Insurance Company, was and still is a corporation, duly organized and existing under and by virtue of the laws of the State of Texas, and at all said times duly authorized by the State of California to engage, and engaged, in doing business in this state as a foreign corporation, and duly licensed to write and issue therein public liability and property damage insurance;

II.

That at all times on the 22nd day of June, 1946, and for a long time prior thereto Allen J. Warner and Robert W. Woodrow were copartners engaged

in transporting property for compensation or hire as a business over public highways in the State of California by means of motor vehicles; that at all [1*] said times the said Allen J. Warner and Robert W. Woodrow were authorized by, and had obtained a permit from, the Railroad Commission of the State of California to operate said business;

III.

That at the time that said permit was granted, said Railroad Commission of the State of California required the said Allen J. Warner and Robert W. Woodrow to procure, and continue in effect during the life of said permit, adequate protection in the form of a policy of public liability and property damage insurance, issued by a company licensed to write such insurance in the State of California, against liability imposed by law upon the said Allen J. Warner and Robert W. Woodrow for the payment of damages for personal bodily injuries in the amount of not less than Five Thousand Dollars (\$5,000) on account of bodily injuries to, or death of, one person; and protection against a total liability of the said Allen J. Warner and Robert W. Woodrow on account of bodily injuries to, or death of, more than one person, as a result of any one accident, in the amount of not less than Ten Thousand Dollars (\$10,000); and protection in an amount of not less than Five Thousand Dollars (\$5,000) for one accident resulting in damage or destruction of property, whether the property of one, or more than one, claimant;

* Page numbering appearing at foot of page of original certified Transcript of Record.

IV.

That pursuant thereto and on the 19th day of April, 1946, in the City and County of San Francisco, State of California, the said Allen J. Warner and Robert W. Woodrow procured from the defendant, and the defendant wrote, executed, and delivered to the said Allen J. Warner and Robert W. Woodrow, said policy of insurance; that said policy of insurance contained all the terms and conditions required by the Railroad Commission of the State of California aforesaid described, and pursuant to the provisions of said policy it remained in full force [2] and effect for a period of one year from and after the said 19th day of April, 1946, and provided therein that defendant would pay in behalf of the said Allen J. Warner and Robert W. Woodrow all sums which they may thereafter become obligated to pay by reason of the liability imposed upon them by law for damages, including damages for care and loss of services, because of bodily injuries sustained by any person or persons, or damages because of injury to or destruction of property, including the loss of use thereof, caused by accident and arising out of the ownership, maintenance, or use of a certain 1939 Dodge Tractor, motor number T78-1665;

V.

That at all times on said 22nd day of June, 1946, the said Allen J. Warner and Robert W. Woodrow were the owners of and in possession of said Dodge Tractor; that on said day the said Allen J. Warner and Robert W. Woodrow were operating

said Dodge Tractor on Public Highway 101 in the County of Humboldt, State of California, at a point about three (3) miles south of the Town of Scotia therein; that at said time and place said Dodge Tractor collided with an automobile in which the plaintiffs were riding, and that by reason thereof the plaintiff, George W. Boulter, sustained certain bodily injuries and property damage, and the plaintiff, Margretta L. Boulter, certain bodily injuries;

VI.

That thereafter, and on the 8th day of August, 1946, the plaintiffs commenced an action in the Superior Court of the State of California, in and for the City and County of San Francisco, against the said Allen J. Warner and Robert W. Woodrow to recover the damages sustained by said plaintiffs that were caused by said bodily injuries and property damage, and that in said action the said Allen J. Warner and Robert W. [3] Woodrow were represented by attorneys hired by the defendant herein; that thereafter and on the 16th day of September, 1947, a judgment was duly given and made by said court in said action that the plaintiff, George W. Boulter, recover the sum of Three Thousand Dollars (\$3,000), and the plaintiff, Margretta L. Boulter, the sum of Two Thousand Dollars (\$2,000), from the said Allen J. Warner and Robert W. Woodrow, together with their costs of suit taxed in the sum of One Hundred Eighteen and 76/100 Dollars (\$118.76), with interest on said judgment at the rate of seven (7) per cent per annum until paid;

VII.

That on said 16th day of September, 1947, written notice of the entry of said judgment was served upon the attorneys for the said Allen J. Warner and Robert W. Woodrow in said action, and that no notice of motion for new trial has ever been filed in said court pertaining to said action, and that no appeal has ever been taken from said judgment or any part thereof, and that said judgment has ever since been and is still in full force and effect, and is now a final judgment; and that no part thereof has ever been paid, and said judgment is wholly unsatisfied;

Wherefore, this plaintiff prays judgment, etc.

SECOND CAUSE OF ACTION

Comes now the plaintiff, Margretta L. Boulter, and complaining of the defendant alleges:

I.

Plaintiff, Margretta L. Boulter, repeats and re-alleges the allegations contained in paragraphs I, II, III, IV, V, VI, and VII of the first cause of action, and hereby incorporates the same by reference herein and makes it a part hereof, as if the same were herein set forth in full; [4]

Wherefore, plaintiffs pray judgment against defendant as follows:

1. That the plaintiff, George W. Boulter, have and recover of and from the defendant the sum of Three Thousand Dollars (\$3,000), with interest thereon at the rate of seven (7) per cent per annum from and after the 16th day of September, 1947.

2. That the plaintiff, Margretta L. Boulter, have and recover of and from the defendant the sum of Two Thousand Dollars (\$2,000), with interest thereon at the rate of seven (7) per cent per annum from and after the 16th day of September, 1947.

3. That the plaintiffs, and each of them, have and recover of and from the defendant the sum of One Hundred Eighteen and 76/100 Dollars (\$118.76), with interest thereon at the rate of seven (7) per cent per annum from and after the 16th day of September, 1947.

4. That the plaintiffs, and each of them, have and recover of and from the defendant their costs of suit herein, and for such other and further relief as to the court may be meet and proper in the premises.

NATHAN G. GRAY,
Attorney for Plaintiffs. [5]

State of California,
County of Alameda—ss.

Nathan G. Gray, being duly sworn, deposes and says:

That he is the attorney for the plaintiffs in the within entitled action; that he has read the foregoing complaint and knows the contents thereof; that the same is true of his own knowledge, except as to matters therein stated on information or belief, and as to those matters that he believes it to be true; that affiant has his office in the County of

Alameda, State of California, and that plaintiffs are absent therefrom, and by reason thereof affiant makes this verification in behalf of said plaintiffs.

/s/ NATHAN G. GRAY.

Subscribed and sworn to before me this 17th day of November, 1947.

(Seal) FLORENCE RICHMOND,
Notary Public in and for the County of Alameda,
State of California.

[Endorsed]: Filed Nov. 19, 1947. Martin Monagan, Clerk.

(Preceding this document is the Certificate to Record on Removal to the District Court of the United States. Following it are the Notice of Intention to File Petition and Bond for Removal of Cause to the United States District Court and of Motion for Order for Such Removal. Petition for Removal of Cause to the United States District Court for the Northern District of California, Southern Division. Memorandum of Points and Authorities in Support of Petition for Removal of Cause to District Court of the United States, Bond on Removal and Order for Removal of Cause, and Affidavit of Service by Mail of Notice of Intention to File Petition, etc.)

[Endorsed]: Filed Jan. 16, 1948. C. W. Calbreath, Clerk. [6]

In the District Court of the United States for the
Northern District of California,
Southern Division

No. 27857-R

GEORGE W. BOULTER and MARGRETTA
L. BOULTER,

Plaintiffs,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant.

ANSWER OF DEFENDANT TO COMPLAINT

Defendant, for its answer to the complaint in the above entitled action, admits, denies and alleges as follows:

AS TO FIRST ALLEGED CAUSE OF ACTION

I.

Defendant admits each and every allegation contained in paragraph I of the first alleged cause of action of said complaint.

II.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraphs II, III and V of the first alleged cause of action of said complaint, and placing its denial thereof upon the ground, defendant denies each and every allegation contained in said paragraphs II, III and V. [7]

III.

Defendant denies each and every allegation contained in paragraph IV of the first alleged cause of action of said complaint.

IV.

Defendant admits each and every allegation contained in paragraph VI of the first alleged cause of action of said complaint, except defendant alleges that the representation of Allen J. Warner and Robert W. Woodrow by attorneys hired by the defendant herein was under and pursuant to a reservation of rights agreement executed by the defendants in said State Court action on or about August 26, 1946. A copy of said reservation of rights agreement is attached to this answer and incorporated herein as though set forth at length, being marked Exhibit "A".

Further, in this connection, defendant alleges that on August 27, 1947, the attorneys for this answering defendant presented a motion to the Superior Court of the State of California, in and for the City and County of San Francisco, for leave to withdraw as attorneys for the defendants Warner and Woodrow in the State Court action brought by George W. Boulter and Margretta L. Boulter; that said motion was denied by said State Court.

V.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the following allegations contained in paragraph VII of the first alleged cause of action of said com-

plaint, and placing its denial thereof upon that ground, defendant denies each and every part of the following allegations:

“and that no part thereof has ever been paid, and said judgment is wholly unsatisfied;” [8]

VI.

As and for a further and separate defense, defendant alleges that:

1.

The only insurance policy that this answering defendant has ever written for Allen J. Warner and Robert W. Woodrow is that certain policy numbered M. C. 170330, copy of which is attached hereto, marked Exhibit “B” and by this reference is incorporated herein as though set forth at length, and which said copy it is alleged contains all of the endorsements and all of the terms and provisions of the insurance contract entered into by and between this defendant and the insureds named in said policy.

2.

In declaration No. 5 in said policy it is provided as follows:

“The Automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation:”

The insured Allen J. Warner, at the time and place mentioned in the complaint in the above entitled action, was engaged in operating that certain

Dodge Tractor referred to in paragraph IV of the first alleged cause of action of said complaint for a purpose other than for the transportation of merchandise, to wit, for the purpose of transporting himself and his family on a vacation trip and for the purpose of carrying himself and his wife home from said vacation trip and at said time and place the said Dodge Tractor was not being used for transportation of merchandise, but was being used in violation of and contrary to the provisions of the above quoted declaration No. 5 in said policy.

3.

That at the time and place of the accident referred to in the complaint herein and at the time of the operation of the Dodge Tractor by Allen J. Warner at the place referred to in paragraph V of the complaint, the said Dodge Tractor was not being operated under the authority of the Highway Carriers' Act of the State of California, Statutes of 1935, Chapter 312, as amended, or the Public Utilities Act of the State of California, Statutes of 1915, Chapter 91, as amended. Further, in this connection, at said time and place of the accident referred to in the complaint herein defendant alleges that said operation of said Dodge Tractor did not arise out of any operations of the insureds under the policy, that was authorized or for which authorization was or is required under the afore-said statutes; and, in this connection, defendant alleges that the said operation at said time and place was for pleasure purposes of the said Allen J. Warner and his wife.

4.

The policy of insurance herein referred to purported to cover only the vehicle described in the policy, to wit, a tractor and trailer, whereas the vehicle involved in the accident referred to in the complaint was a tractor only, for which no insurance was provided under said contract.

5.

Defendant alleges that at the time and place of the accident referred to in the complaint the said Allen J. Warner was driving the Dodge Tractor referred to in the complaint on a pleasure trip, which said trip commenced in San Francisco and was for the purpose of conveying the said Allen J. Warner's mother and son to Willow Creek, California, for the purpose of a visit with his sister at said place; that accompanying [10] said Allen J. Warner on said trip was his wife and as an additional purpose of said trip the said Allen J. Warner was intending to spend a week at Willow Creek on his vacation; that the accident referred to in the complaint happened on the return trip from Willow Creek to San Francisco, at which time the sole purpose of the use of said tractor was to get the said Allen J. Warner and his family back to San Francisco from a vacation trip.

VII.

As and for a further and separate defense, defendant alleges that heretofore on October 18, 1946, defendant filed a complaint for declaratory relief in the District Court of the United States for the Northern District of California, Southern

Division, entitled Commercial Standard Insurance Company, a corporation, Plaintiff, vs. George W. Boulter, Margretta L. Boulter, Allen J. Warner, Robert W. Woodrow, First Doe, Second Doe and Third Doe, Defendants, Numbered therein 26533 G. In said complaint this answering defendant was the plaintiff and the plaintiffs George W. Boulter and Margretta L. Boulter in this action were named as defendants along with the insureds named in the insurance policy referred to in the complaint in this action. In the complaint in the Federal Court action this answering defendant asked for a declaratory judgment against the defendants in said action and for a decree establishing that the Commercial Standard Insurance Company was not obligated to pay any judgment that might be rendered against Allen J. Warner and/or Robert W. Woodrow on account of the accident referred to in the complaint herein. Said complaint in the Federal Court action also asked for a decree that the insurance policy referred to in the above entitled action did not cover the accident of June 22, 1946 between the Dodge Tractor referred to in the complaint on file herein and the [11] automobile of George W. Boulter, and further asking for a decree declaring that the endorsement prescribed by the Railroad Commission of the States of California on said policy of insurance had no application to the accident of June 22, 1946, described in the complaint herein, or to any claims arising therefrom.

That the District Court of the United States for

the Northern District of California, Southern Division, by a judgment duly given and made and duly entered on the 14th day of August, 1947, decreed as follows:

“It appears to the Court and the Court finds that summons and complaint in this cause has been duly and properly served upon the defendant Allan J. Warner and that said Allan J. Warner has failed to appear in this action within the time allowed by law and that said defendant is now in default, said default having heretofore been duly entered at the request of the plaintiff.

The plaintiff having heretofore appeared before this Court on Monday, August 11th, 1947, by its counsel Cooley, Crowley, Gaither and Dana through Leighton M. Bledsoe, of counsel, and having on said date presented its motion for a default judgment, and evidence both oral and documentary having been presented, and the Court being fully advised now finds the allegations of the complaint for declaratory relief are true, and decrees as follows:

It is hereby ordered, adjudged and decreed that plaintiff's motion for a default judgment against defendant Allan J. Warner be, and the same is hereby granted.

It is further ordered, adjudged and decreed as follows:

1. That plaintiff's insurance policy No. MC 170330 does not cover the accident which occurred on June 22, 1946 in Humboldt County, California between the Dodge Tractor driven by Allan J.

Warner and the automobile driven by George W. Boulter.

2. That the named assureds under the plaintiff's insurance policy No. MC 170330 are not entitled to any benefits under or by virtue of said policy of insurance with reference to the said accident of June 22, 1946.

3. That the plaintiff is not obligated to afford any defense to its named insureds under policy No. MC 170330 in any action arising out [12] of the accident described in the complaint filed in the above entitled action.

4. That plaintiff is not obligated to pay any judgment that may be obtained or rendered against the named insureds in policy No. MC 170330 by virtue of any claim or complaint arising out of the accident of June 22, 1946 as described in the complaint.

5. That the endorsement prescribed by the Railroad Commission of the State of California has no application to the accident of June 22, 1946 described in the complaint or to any claims arising therefrom.

Dated: August 14, 1947.

LOUIS E. GOODMAN,
Judge of the District Court of the United States."

That the District Court of the United States for the Northern District of California, Southern Division, by a judgment duly given and made and duly entered on the 27th day October, 1947, decreed as follows:

“It appears to the Court and the Court finds that summons and complaint in this cause has been duly and properly served upon the defendant Robert W. Woodrow and that said Robert W. Woodrow has failed to appear in this action within the time allowed by law and that said defendant is now in default, said default having heretofore been duly entered at the request of the plaintiff.

The plaintiff having heretofore appeared before this Court on Monday, October 27, 1947, by its counsel Cooley, Crowley, Gaither & Dana through Rogers P. Smith, of Counsel, and having on said date presented its motion for a default judgment, and the Court being fully advised now finds the allegations of the complaint for declaratory relief are true and decrees as follows:

It is hereby ordered, adjudged and decreed that plaintiff's motion for a default judgment against defendant Robert W. Woodrow be, and the same is hereby granted.

It is further ordered, adjudged and decreed as follows:

1. That Plaintiff's insurance policy No. MC 170330 does not cover the accident which occurred on June 22, 1946, in Humboldt County, California between the Dodge Tractor driven by Allen J. Warner and the automobile driven by George W. Boulter.

2. That the named assureds under the plaintiff's insurance policy No. MC 170330 are not entitled to

[13] any benefits under or by virtue of said policy of insurance with reference to the said accident of June 22, 1946.

3. That the plaintiff is not obligated to afford any defense to its named insureds under policy No. MC 170330 in any action arising out of the accident described in the complaint filed in the above entitled action.

4. That plaintiff is not obligated to pay any judgment that may be obtained or rendered against the named insureds in policy No. MC 170330 by virtue of any claim or complaint arising out of the accident of June 22, 1946, as described in the complaint.

5. That the endorsement prescribed by the Railroad Commission of the State of California has no application to the accident of June 22, 1946 described in the complaint or to any claims arising therefrom.

Dated: October 27, 1947.

LOUIS E. GOODMAN,

Judge of the District Court of the United States.”

That the said Allen J. Warner and Robert W. Woodrow referred to in the foregoing decrees are the same parties referred to in the complaint herein and referred to in the insurance policy mentioned in the complaint herein.

That by reason of the foregoing declaratory judgments the question of this answering defendant's liability under the insurance policy sued on herein has become *res adjudicata*; that said judg-

ments are, and each of them is, a complete and final determination of the issues herein against the plaintiffs in the above entitled action and said decrees operate as a bar to the above entitled action.

During the pendency of the State Court action referred to in the complaint herein as against Allen J. Warner and Robert W. Woodrow, the plaintiffs in said State Court action George W. Boulter and Margretta L. Boulter were represented by their attorney Nathan G. Gray, who is a resident of Alameda County with offices in Berkeley, California; that while said State Court action was pending the above described declaratory relief action was also pending in the District Court of the United [14] States, herein described. On or about October 17, 1946, this answering defendant's attorneys in San Francisco notified attorney Nathan G. Gray by letter of the filing of said declaratory relief action in the Federal Court and of the joinder therein as defendants of George W. Boulter and Margretta L. Boulter. Mr. Gray was also requested by said letter to accept service of summons and complaint in the declaratory relief action on behalf of his clients. On October 19, 1946, these answering attorneys forwarded to said Nathan G. Gray a copy of the complaint for declaratory relief herein referred to; that said attorneys received a letter from attorney Gray, dated October 18, 1946, advising that he would communicate with his clients and request permission to appear in their behalf in the declaratory relief action and again on October 28, 1946 said attorney Gray wrote to the attorneys

for this defendant stating that he would ask the permission of his clients to appear in their behalf and asking for authorities to support the declaratory relief action; that said authorities were supplied to said attorney Gray by letter of November 8, 1946. On December 5, 1946, defendant's attorneys requested by letter to attorney Gray that he file an appearance in the Federal Court on behalf of his clients and stating that if he was not willing to do this to return the copy of the complaint so that it could be used to place in the hands of the United States Marshal for service on Mr. Gray's clients; that said copy of the complaint was never returned by Mr. Gray; that thereafter on January 16, 1947, Mr. Gray requested defendant's attorney to postpone the hearing on the motion of Commercial Standard Insurance Company for an injunction to enjoin the State Court proceedings and this request for a continuance was granted. On February 18, 1947, defendant's attorneys sent a letter to attorney Gray stating that it was understood by them that he had authority to file an appearance for his clients in the [15] declaratory relief action and requesting him to do so; that no denial was ever made of said statement in said letter and no answer was made thereto by the said attorney Gray. On April 29, 1947, defendant's attorneys advised attorney Gray that they intended to proceed against the parties served in the declaratory relief action and to secure a declaratory judgment therein; that during all of the times herein mentioned the said Nathan Gray was acting as the attorneys for plain-

tiffs in the above entitled action and was authorized and empowered to act on their behalf as such attorney with reference to the matters hereinabove referred to; that by reason of the foregoing the plaintiffs herein were advised and had knowledge of the pendency of the declaratory relief action herein referred to and of the issues involved therein; that by reason of the foregoing said plaintiffs are estopped to deny the full force and effect of the declaratory judgments hereinabove described as *res adjudicata* against them, and each of them.

AS TO SECOND ALLEGED CAUSE OF
ACTION

I.

For its answer to paragraph I of the second alleged cause of action of said complaint, defendant hereby repeats and makes a part hereof all of its foregoing admissions, denials, allegations and separate defenses contained in its foregoing answer to the first alleged cause of action of said complaint.

Wherefore, defendant prays that plaintiffs, or either of them, take nothing herein and that defendant have judgment for its costs of suit herein incurred.

/s/ PAUL C. DANA,

/s/ LEIGHTON M. BLEDSOE,

/s/ ROGERS P. SMITH,

/s/ DANA, BLEDSOE & SMITH,
Attorneys for Defendant. [16]

State of California,
City and County of San Francisco—ss.

Leighton M. Bledsoe, being first duly sworn, deposes and says:

That he is a member of the law firm of Dana, Bledsoe & Smith, which law firm has its offices at 440 Montgomery Street, San Francisco, California; that said Dana, Bledsoe & Smith are the attorneys for the defendant; that all of the officers of said defendant are absent from said City and County of San Francisco, where affiant has his and said law firm have their offices, and for that reason affiant makes this verification for and on behalf of defendant; that affiant has read the foregoing answer and knows the contents thereof; that the same is true of his own knowledge, except as to such matters which are therein stated on his information or belief; and as to such matters he believes the same to be true.

Subscribed and sworn to before me this 19th day of January, 1948.

LEIGHTON M. BLEDSOE,

(Seal) /s/ DOROTHY N. McLENNAN,
Notary Public in and for the City and County of
San Francisco, State of California. [17]

EXHIBIT "A"

San Francisco, California

August 26, 1946

Commercial Standard Insurance Co.

Fort Worth, Texas

c/o Cooley, Crowley, Gaither & Dana,

206 Sansome Street

San Francisco, California

Re: George W. Boulter and Margretta

Boulter v. Allan J. Warner, Robert

W. Woodrow, et al.—

San Francisco Superior Court No. 256235

Comm. Stand. Ins. Pol. No. MC 170330

Gentlemen:

This is to advise you that we, and each of us, agree that you, and any of your representatives and attorneys, may participate in any investigation and/or defense of the above mentioned claim by George W. Boulter and Margretta Boulter, and of that certain action numbered 356235 in the Superior Court of the State of California in and for the City and County of San Francisco brought by said Boulders against us; and that any such action taken or to be taken by you, or any of your representatives, is entirely without prejudice to any rights and defenses of the Commercial Standard Insurance Company under the above described, and any, insurance contract; and any such participation does not and shall not constitute an admis-

sion of liability on the part of said Commercial Standard Insurance Company.

It is likewise understood by us, and each of us, that nothing herein contained shall prejudice the right of either the Commercial Standard Insurance Company or of the undersigned to apply to any court of competent jurisdiction at any time for a determination of the rights of the parties with respect to said, or any, contract of insurance.

We do, and each of us hereby does, waive any right that we, or either of us, may have to claim that the Commercial Standard Insurance Company waives, has waived, or shall waive any right to deny liability under said, and any, contract of insurance. At the same time, we in no way waive any of our rights against the Commercial Standard Insurance Company under said contract.

Very truly yours,

ALLEN J. WARNER,
ROBERT W. WOODROW. [18]

EXHIBIT "B"

AUTOMOBILE LIABILITY POLICY PUBLIC
TRANSPORTATION FORM

M. C. Series 170,001 to 172,000.

Commercial Standard Insurance
Company

Fort Worth, Texas

DECLARATIONS

1. Name of insured: Allen J. Warner and Robert W. Woodrow.

2. Address of insured: No. 10, Ord Court, San Francisco, California.

3. The Insured is: Partnership. Insured's business is: Trucking.

4. The term of this policy begins at 12:01 a.m., April 19, 1946, and ends at 12:01 a.m. April 19, 1947, standard time as to both dates, at the place where this policy is countersigned.

5. The Automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation:

6. Description of the automobiles or vehicles to which this insurance relates:

Year Model: 1939. Trade Name: Dodge. Type of Body (if trailer—2 or 4 wheel): Tractor. Motor Number, Serial Number: M No. T78-1665, S No. 8702218. Annual B. I. Prem.: \$220.00. Annual P. D. Prem.: \$110.00. Annual Total: \$330.00.

Exhibit "B"—(Continued)

Total Annual Premium: B. I. Prem. \$220.00;
P. D. Prem.: \$110.00. Total: \$330.00.

Railroad Commission Endorsement Attached to
Policy.

349R

REVISED PREMIUM PAYMENT
AGREEMENT

It is hereby understood and agreed that the premium under the policy of which this endorsement is issued to become a part is payable as follows:

Unpaid balance	\$ 66.00
Additional return premium.....	145.53
Balance due	211.53

Balance due shall be payable \$29.10 cash and remainder in 2 equal monthly installments of \$91.21 on or before the 19th day of each succeeding month beginning November, 1946. In case of any change in the premium the unpaid installments shall be adjusted accordingly.

If the Company shall cancel this policy due to failure of the Insured to pay any installment as and when due, such cancellation shall be at the customary short rates.

Subject to all the conditions, limitations and agreements of the policy as written, except as herein specifically provided.

Attached to and forming a part of Policy No. MC 170330 of the Commercial Standard Insurance Company.

Exhibit "B"—(Continued)

If this endorsement is not attached to the Policy at the time the Policy is issued, it is necessary that the Insured sign below.

Accepted:

.....
Insured.

.....
Agent.

Dated at San Francisco, California, this 26th day of November, 1946.

End. 349-R.

305

Name of Insured: Robert W. Woodrow.

In consideration of an additional premium of One Hundred Forty Five and 53/100 Dollars, (\$145.53) it is hereby understood and agreed that the following equipment shall be added to the undermentioned policy on a 300 mile radius:

1-1935 Ward La France Truck M 9521.

2-1932 Pacific Full Trailer S 349.

Ann Prem.

Add. Pro Rate

PL \$220.00

PL \$97.02

PD \$110.00

PD \$48.51

This endorsement shall take effect on the 8th day of November, 1946, 12:01 a.m., and shall terminate with this policy.

Nothing herein contained shall vary, alter, waive or extend any of the terms, warranties, conditions

Exhibit "B"—(Continued)

or agreements of the policy, except as herein specifically provided.

Attached to and forming a part of Policy No. MC 170330 of the Commercial Standard Insurance Company.

Dated at San Francisco, California, this 26th day of November, 1946.

.....
Agent.

Endorsement 305

349

It is hereby understood and agreed that the premium under the policy of which this endorsement is issued to become a part is payable as follows:

Cash on Delivery of Policy: \$68.00.

Handling Charge: \$2.00 Inc.

Balance Due: \$264.00.

Balance due shall be payable in 8 equal monthly installments of \$33.00 on or before the 19th day of each succeeding month beginning May, 1946. In case of any change in the premium the unpaid installments shall be adjusted accordingly.

If the Company shall cancel this policy due to failure of the Insured to pay any installment as and when due, such cancellation shall be at the customary short rates.

Subject to all the conditions, limitations and agreements of the policy as written, except as herein specifically provided.

Exhibit "B"—(Continued)

Attached to and forming a part of Policy No. MC 170330 of the Commercial Standard Insurance Company.

If this endorsement is not attached to the Policy at the time the Policy is issued, it is necessary that the Assured sign below.

Accepted:

.....

Insured.

.....

Agent.

Dated at San Francisco, California, this 19th day of April, 1946.

End. 349

7. The liability of the Company shall be limited to Five Thousand Dollars (\$5,000.00) for one person injured or killed, and, subject to that limit for each person injured or killed, the Company's liability on account of any one accident shall be limited to Ten Thousand Dollars (\$10,000.00). The liability of the Company shall be limited to Five Thousand Dollars (\$5,000.00) on account of claims for damages to or destruction of property in any one accident.

In witness whereof, the Commercial Standard Insurance Company has caused this policy to be signed by its president and secretary at Fort Worth, Texas, and countersigned on the declara-

Exhibit "B"—(Continued)

tions page by a duly authorized representative of the company.

/s/ KARL F. VASIN,
President.

/s/ R. E. BURSON,
Secretary.

Countersigned at This
day of, 19...., by,
Representative.

Commercial Standard Insurance Company
Fort Worth, Texas

(A stock insurance company, herein called
the company)

Agrees with the insured, named in the declarations made a part hereof, in consideration of the payment of the premium and in reliance upon the statements in the declarations and subject to the limits of liability, exclusions, conditions and other terms of this policy:

INSURING AGREEMENTS

I. Coverage A—Bodily Injury Liability

To pay on behalf of the insured all sums which the insured shall become obligated to pay by reason of the liability imposed upon him by law for damages, including damages for care and loss of services, because of bodily injury, including death at any time resulting therefrom, sustained by any per-

Exhibit "B"—(Continued)

son or persons, caused by accident and arising out of the ownership, maintenance or use of the automobile, including the loading and unloading thereof.

Coverage B—Property Damage Liability

To pay on behalf of the insured all sums which the insured shall become obligated to pay by reason of the liability imposed upon him by law for damages because of injury to or destruction of property, including the loss of use thereof, caused by accident and arising out of the ownership, maintenance or use of the automobile, including the loading and unloading thereof.

Special Agreements

In consideration of the premium at which this policy is written the following special agreements are made a part of said policy:

(a) The terms of any special endorsement required by law or legal regulation or by any government authority to be attached to this policy shall apply only to accidents occurring within the boundaries of the State or jurisdiction whose laws or authorities require said endorsement.

(b) If one or more copies of this policy are or shall be issued, the liability of the Company under all policies shall not be increased by this fact and the total liability of this Company under all policies combined shall be limited to the amounts shown in each policy.

(c) As between the Insured and the Company the terms of this policy shall govern as though the endorsement or endorsements prescribed and re-

Exhibit "B"—(Continued)

quired under the provisions of the laws or regulations of any State or States or of the United States were not attached; and in consideration of the attachment of said endorsement or endorsements at the request of the Insured, the Insured agrees that if the Company shall be obliged to pay any claim which it would not have been required to pay except for said endorsement or endorsements the Insured named in this policy shall reimburse the Company for any and all sums and disbursements of every kind, including loss payments, costs and expenses, which it shall have paid in connection with such claims, plus expenses incurred by the Company in enforcing the terms of the agreement contained in this Clause C.

II. Defense, Settlement, Supplementary Payments

As respects such insurance as is afforded by the other terms of this policy under coverages A and B the company shall

(a) defend in his name and behalf any suit against the insured alleging such injury or destruction and seeking damages on account thereof, even if such suit is groundless, false or fraudulent; but the company shall have the right to make such investigation, negotiation and settlement of any claim or suit as may be deemed expedient by the company; (b) pay all premiums on bonds to release attachments for an amount not in excess of the applicable limit of liability on this policy, all premiums on appeal bonds required in any such defended suit,

Exhibit "B"—(Continued)

but without any obligation to apply for or furnish such bonds, all costs taxed against the insured in any such suit, all expenses incurred by the company, all interest accruing after entry of judgment until the company has paid, tendered or deposited in court such part of such judgment as does not exceed the limit of the company's liability thereon, and expenses incurred by the insured, in the event of bodily injury, for such immediate medical and surgical relief to others as shall be imperative at the time of accident;

(c) reimburse the insured for all reasonable expenses, other than loss of earnings, incurred at the company's request.

The company agrees to pay the amounts incurred under this insuring agreement, except settlements of claims and suits, in addition to the applicable limit of liability of this policy.

Bail Bond Expense

The company shall pay the cost of bonds, but without obligation to apply for or furnish such bonds, guaranteeing the insured's appearance in court if such appearance is required by reason of an accident or traffic law violation occurring during the policy period and arising out of the use of an automobile with respect to which use insurance is afforded such insured under coverage A of this policy. The company's liability under this insuring agreement with respect to each bond shall not exceed the usual charges of surety companies for such bond nor \$100.

Exhibit "B"—(Continued)

III. Automobile Defined, Trailers, Two or More Automobiles

Except where specifically stated to the contrary, the word "automobile" wherever used in this policy shall mean the motor vehicle, trailer or semi-trailer described in this policy. The word "trailer" shall include semitrailer.

When two or more automobiles are insured hereunder, the terms of this policy shall apply separately to each but a motor vehicle and a trailer or trailers attached thereto shall be held to be one automobile as respects limits of liability under coverages A and B.

IV. Temporary Use of Substitute Automobile

While an automobile owned in full or in part by the named insured is withdrawn from normal use because of its breakdown, repair, servicing, loss or destruction, such insurance as is afforded by this policy with respect to such automobile applies with respect to another automobile not so owned while temporarily used as the substitute for such automobile. This insuring agreement does not cover as an insured the owner of the substitute automobile or any employee of such owner.

V. Automatic Insurance for Newly Acquired Automobiles

If the named insured who is the owner of the automobile acquires ownership of another automobile and so notifies the company within thirty days following the date of its delivery to him, such insurance as is afforded by this policy applies also

Exhibit "B"—(Continued)

to such other automobile as of such delivery date:

(a) if it replaces an automobile described in this policy, but only to the extent the insurance is applicable to the replaced automobile, or

(b) if it is an additional automobile and if the company insures all automobiles owned by the named insured at such delivery date, but only to the extent the insurance is applicable to all such previously owned automobiles.

This insuring agreement does not apply: (a) to any loss against which the named insured has other valid and collectible insurance, or (b) except during the policy period, but if such delivery date is prior to the effective date of this policy, the insurance applies as of such effective date.

The named insured shall pay an additional premium required because of the application of the insurance to such other automobile. The insurance terminates upon the replaced automobile on such delivery date.

VI. Policy Period, Territory, Purposes of Use

This policy applies only to accidents which occur during the policy period, while the automobile is within the United States of America, and is owned, maintained and used for the purpose stated as applicable thereto in Statement 5 of the declarations.

EXCLUSIONS

This policy does not apply:

(a) while the automobile is used for transportation of persons for a consideration, unless such use

Exhibit "B"—(Continued)

is specifically declared and described in this policy and premium charged therefor; or while rented, leased or hired;

(b) to liability assumed by the insured under any contract or agreement;

(c) while the automobile is used for the towing of any trailer owned or hired by the named insured and not covered by like insurance in the company; or while any trailer covered by this policy is used with any automobile owned or hired by the named insured and not covered by like insurance in the company;

(d) to bodily injury to or death of any employee of the insured while engaged in the employment of the insured, or while engaged in the operation, maintenance or repair of the automobile;

(e) under coverage A, to any obligation for which the insured or any company as his insurer may be held liable under any workmen's compensation law;

(f) under coverage B, to injury to or destruction of property owned by, rented to, in charge of or transported by the insured;

(g) while being driven or operated by any persons other than the insured or his paid employee;

(h) to liability for loss or expenses resulting from fire or explosion occurring within the contents of any vehicle (whether such contents be loaded or unloaded) or from leakage of such contents, except contents of the ordinary fuel tank containing fuel for the propulsion of the described automobile only.

Exhibit "B"—(Continued)

CONDITIONS

1. Limits of Liability—Coverage A

The limit of bodily injury liability stated in the declarations as applicable to "one person" is the limit of the company's liability for all damages, including damages for care and loss of services, arising out of bodily injury, including death at any time resulting therefrom, sustained by one person in any one accident; the limit of such liability stated in the declarations as applicable to "one accident" is, subject to the above provision respecting each person, the total limit of the company's liability for all damages, including damages for care and loss of services, arising out of bodily injury, including death at any time resulting therefrom, sustained by one person in any one accident; the limit of such liability stated in the declarations as applicable to "one accident" is, subject to the above provision respecting each person, the total limit of the company's liability for all damages, including damages for care and loss of services, arising out of bodily injury, including death at any time resulting therefrom, sustained by two or more persons in any one accident.

2. Limits of Liability

The inclusion herein of more than one insured shall not operate to increase the limits of the company's liability. A disaster or series of accidents arising from one and the same cause, shall be considered one accident within the meaning of this policy.

Exhibit "B"—(Continued)

3. Assault and Battery

Assault and battery shall be deemed an accident unless committed by or at the direction of the insured.

4. Notice of Accident

When an accident occurs written notice shall be given by or on behalf of the insured to the company or any of its authorized agents as soon as practicable. Such notice shall contain particulars sufficient to identify the insured and also reasonably obtainable information respecting the time, place and circumstances of the accident, the names and addresses of the injured and of available witnesses.

5. Notice of Claim or Suit

If claim is made or suit is brought against the insured, the insured shall immediately forward to the company every demand, notice, summons or other process received by him or his representative.

6. Assistance and Cooperation of the Insured

The insured shall cooperate with the company and, upon the company's request, shall attend hearings and trials and shall assist in effecting settlements, securing and giving evidence, obtaining the attendance of witnesses and in the conduct of suits. The insured shall not, except at his own cost, voluntarily make any payment, assume any obligation or incur any expense other than for such immediate medical and surgical relief to others as shall be imperative at the time of accident.

7. Action Against Company

Exhibit "B"—(Continued)

No action shall lie against the company unless, as a condition precedent thereto, the insured shall have fully complied with all the terms of this policy, nor until the amount of the insured's obligation to pay shall have been finally determined either by judgment against the insured after actual trial or by written agreement of the insured, the claimant and the company.

Any person or organization or the legal representative thereof who has secured such judgment or written agreement shall thereafter be entitled to recover under this policy to the extent of the insurance afforded by this policy. Nothing contained in this policy shall give any person or organization any right to join the company as a co-defendant in any action against the insured to determine the insured's liability.

Bankruptcy or insolvency of the insured or of the insured's estate shall not relieve the company of any of its obligations hereunder.

8. Other Insurance

If the insured has other insurance against a loss covered by this policy the company shall not be liable under this policy for a greater proportion of such loss than the applicable limit of liability stated in the declarations bears to the total applicable limit of liability of all valid and collectible insurance against such loss; provided, however, the insurance under Insuring Agreement IV shall be excess insurance over any other valid and collectible insurance available to the insured, either as an

Exhibit "B"—(Continued)

insured under a policy applicable with respect to the automobile or otherwise, against a loss covered under said insuring agreement.

9. Subrogation

In the event of any payment under this policy, the company shall be subrogated to all the insured's rights of recovery therefor against any person or organization and the insured shall execute and deliver instruments and papers and do whatever else is necessary to secure such rights. The insured shall do nothing after loss to prejudice such rights.

10. Changes

Notice to any agent or knowledge possessed by any agent or by any other person shall not effect a waiver or a change in any part of this policy or estop the company from asserting any right under the terms of this policy; nor shall the terms of this policy be waived or changed, except by endorsement issued to form a part of this policy, signed by a duly authorized representative of the company.

11. Assignment

Assignment of interest under this policy shall not bind the company until its consent is endorsed hereon; if, however, the named insured shall die or be adjudged bankrupt or insolvent within the policy period, this policy, unless canceled, shall, if written notice be given to the company within sixty days after the date of such death or adjudication, cover (1) the named insured's legal representative as the named insured, and (2) any per-

Exhibit "B"—(Continued)

son having proper temporary custody of the automobile, as an insured, until the appointment and qualification of such legal representative but in no event for a period of more than sixty days after the date of such death or adjudication.

12. Statutory Provisions

If any of the terms or conditions of this policy conflict with the law of the State in which this policy is issued, such conflicting terms or conditions shall be inoperative in such State insofar as they are in conflict with such law. Any specific statutory provision in force in the State in which this policy is issued shall supersede any condition of this policy inconsistent therewith.

13. Cancellation

This policy may be canceled by the named insured by mailing to the company written notice stating when thereafter such cancellation shall be effective. This policy may be canceled by the company by mailing to the named insured at the address shown in this policy written notice stating when not less than five days thereafter such cancellation shall be effective. The mailing of notice as aforesaid shall be sufficient proof of notice and the effective date and hour of cancellation stated in the notice shall become the end of the policy period, provided, however, that such date and hour of cancellation shall conform to, and, where different, be reformed to coincide with the date and hour of cancellation effective as to any government authority to which under the terms of this policy or any

Exhibit "B"—(Continued)

endorsement hereto notice is required for cancellation. Delivery of such written notice either by the named insured or by the company shall be equivalent to mailing.

A cancellation of this policy effected through the issuance of notice by the company because of the failure of named insured to pay any premium or to make any report which is required in this policy or any endorsement hereto shall be deemed to be a cancellation at the instance of and by the named insured, provided said notices of cancellation are not issued earlier than ten days after the due date as to said premium or report.

If the named insured cancels, earned premiums shall be computed in accordance with the customary short rate table and procedure. If the company cancels, earned premiums shall be computed pro rata. Premium adjustment may be made at the time cancellation is effected and, if not then made, shall be made as soon as practicable after cancellation becomes effective. The company's check or the check of its representative mailed or delivered as aforesaid shall be sufficient tender of any refund of premium due to the named insured.

14. Declarations

By acceptance of this policy the named insured agrees that the statements in the Declarations are his agreements and representations, that this policy is issued in reliance upon the truth of such representations and that this policy embodies all agreements existing between himself and the company or any of its agents relating to this insurance.

Exhibit "B"—(Continued)

AFFIDAVIT OF COPY

Name of Assured: Allen J. Warner and Robert W. Woodrow.

State of Texas,

County of Tarrant—ss.

On this day before the undersigned authority personally appeared J. S. Pieringer, Jr., who, after being sworn, deposes and states that he is Secretary for the Commercial Standard Insurance Company of Fort Worth, Texas, and that this is a true and correct copy of Policy Number MC 170330 issued for this assured.

/s/ J. S. PIERINGER, JR.

Subscribed and sworn to before me this 15th day of January, A. D. 1948.

(Seal) /s/ KATHLEEN PAYNE,

Notary Public in and for Tarrant County, Texas.

[Endorsed]: Filed Jan. 19, 1948. [24]

[Title of District Court and Cause.]

DEMAND FOR TRIAL BY JURY

Notice is hereby given that the above named plaintiffs do hereby demand a trial by jury of all issues triable by jury in the above entitled cause.

Dated: January 20, 1948.

NATHAN G. GRAY,

Attorney for Plaintiffs.

(Affidavit of Service by Mail.)

[Endorsed]: Filed Jan. 21, 1948. [25]

[Title of District Court and Cause.]

REQUEST FOR ADMISSION OF FACTS

The plaintiffs above named, pursuant to Rule 36 of the Federal Rules of Civil Procedure, do hereby request that the above named defendant admit the truth of each and all of the following relevant matters of fact:

1. That the policy of insurance referred to in the Answer of Defendant to Complaint as Exhibit "B" had attached to it and effective at all times on the 22nd day of June, 1946, an endorsement entitled, "Standard Form of Endorsement Prescribed by the Railroad Commission of the State of California", numbered 379, a copy of which is attached to the complaint of the plaintiff in that certain action pending in this court in which the defendant herein is the plaintiff and the plaintiffs herein are some of the defendants, numbered 26533 G in the records of the above entitled court.

2. That on the 22nd day of June, 1946, at the time of the accident described in paragraph V of the Complaint on file herein, Allen J. Warner and Robert W. Woodrow were the [26] owners of that certain 1939 Dodge Tractor Motor numbered T78-1665.

3. That on said 22nd day of June, 1946, and at

the time of said accident said 1939 Dodge tractor was being operated by the said Allen J. Warner.

Dated: March 10, 1948.

NATHAN G. GRAY,
Attorney for Plaintiffs.

(Affidavit of Service by Mail.)

[Endorsed]: Filed Mar. 11, 1948. [27]

[Title of District Court and Cause.]

STATEMENT OF DEFENDANT COMMERCIAL STANDARD INSURANCE COMPANY
IN REPLY TO PLAINTIFFS' REQUEST
FOR ADMISSION OF FACTS

Comes now the defendant Commercial Standard Insurance Company and, pursuant to the provisions of Rule 36, Rules of Civil Procedure admits, denies and alleges as follows with respect to the "Request For Admission Of Facts" served upon said defendant on the 11th day of March, 1948:

1. With respect to the demand for admission of facts contained in Paragraph 1 of said request, this defendant admits all of the statements therein contained except that this defendant denies that said "Standard Form of Endorsement Prescribed by the Railroad Commission of the State of California" was effective at any time on the 22nd day of June, 1946, and this defendant alleges and states further that the policy of insurance referred to in the answer filed herein by this defendant, and at-

tached to said [28] answer as Exhibit "B" thereof, was wholly ineffective at all times on the 22nd day of June, 1946, and that said policy and said rider did not attach to, and did not cover said 1939 Dodge tractor at the time and place of the accident referred to in this action.

2. This defendant admits the facts stated in Paragraphs 2 and 3 of said request for admission of facts.

Dated: March 18, 1948.

/s/ PAUL C. DANA,
/s/ LEIGHTON M. BLEDSOE,
/s/ ROGERS P. SMITH,
/s/ DANA, BLEDSOE & SMITH,
Attorneys for Defendant. [29]

State of California,
City and County of San Francisco—ss.

Leighton M. Bledsoe, being first duly sworn, deposes and says:

That he is a member of the law firm of Dana, Bledsoe & Smith, which law firm has its offices at 440 Montgomery Street, San Francisco, California; that affiant and said Dana, Bledsoe & Smith are attorneys for the defendant in this action; that all of the officers of said defendant are absent from said City and County of San Francisco, where affiant and said law firm have their offices, and for that reason affiant makes this verification for and on behalf of the defendant; that affiant has read the foregoing statement and knows the contents

thereof; that the same is true of his own knowledge, except as to such matters which are therein stated on his information or belief; and as to such matters he believes the same to be true.

/s/ LEIGHTON M. BLEDSOE.

Subscribed and sworn to before me this 19th day of March, 1948.

(Seal) /s/ JAMES S. MULVEY,

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: Filed Mar. 20, 1948. [30]

[Title of District Court and Cause.]

VERDICT

We, the Jury, find in favor of the Plaintiffs and assess the damages against the Defendant in the sum of \$3,000.00 on behalf of the Plaintiff George W. Boulter, and \$2,000.00 on behalf of the Plaintiff Margretta L. Boulter, and on behalf of both in the sum of \$118.76, with interest on all above amounts at the rate of 7% per annum from September 16, 1947.

WM. J. LIEBHARDT,
Foreman.

July 7, 1948.

[Endorsed]: Filed July 7, 1948, at 5:15 p.m. [31]

47a *G. W. Boulter and M. L. Boulter vs.*

In the Southern Division of the United States
District Court for the Northern District
of California

No. 27857-R

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Plaintiffs,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant.

JUDGMENT ON VERDICT

This cause having come on regularly for trial on July 6, 1948, being a day in the March, 1948 Term of this Court, before the Court and a Jury of twelve persons duly impaneled and sworn to try the issues joined herein; Nathan G. Gray, Esq., appearing as attorney for the plaintiffs, and Robert Cathcart, Esq., appearing as attorney for the defendant, and the trial having been proceeded with on the 6th and 7th days of July in said year and term, and oral and documentary evidence on behalf of the respective parties having been introduced and closed, and the cause, after arguments by the attorneys and the instructions of the Court, having been submitted to the Jury and the Jury having subsequently rendered the following verdict, which was ordered recorded, viz: "We, the Jury, find in favor of the Plaintiffs and assess the damages against the Defendant in the sum

of \$3,000.00 on behalf of the Plaintiff George W. Boulter, and \$2,000.00 on behalf of the Plaintiff Margretta L. Boulter, and on behalf of both in the sum of \$118.76, with interest on all above amounts at the rate of 7% per annum from September 16, 1947. Wm. J. Liebhardt, Foreman," and the Court having ordered that judgment be entered herein in accordance with said verdict and for costs;

Now, therefore, by virtue of the law and by reason of the premises aforesaid, it is considered by the Court that said plaintiffs do have and recover of and from said defendant the sums set out above, together with their costs herein expended taxed at \$.....

Judgment filed this 8th day of July, 1948.

/s/ C. W. CALBREATH,
Clerk.

Entered in Civil Docket July 9, 1948.

[Endorsed]: Filed July 8, 1948.

[Title of District Court and Cause.]

MOTION OF DEFENDANT FOR JUDGMENT
NOTWITHSTANDING THE VERDICT
AND IN THE ALTERNATIVE
FOR A NEW TRIAL

Comes the defendant, Commercial Standard Insurance Company, a corporation, and files its motion praying that the jury's verdict herein and the judgment rendered and entered thereon be set aside and judgment entered herein for the defendant notwithstanding the verdict, and its motion for a new trial in the alternative, and as grounds therefor states:

A.

The motion for judgment notwithstanding the verdict should be granted for the following reasons:

1. The verdict was contrary to law;
2. The verdict was contrary to the evidence;
3. The verdict was contrary to the law and the evidence; [32]
4. The Court erred in refusing to direct a verdict for the defendant;
5. There was no evidence that, at the time of the accident referred to in the complaint, the tractor described in the policy referred to in the complaint was being used for the transportation of merchandise.

B.

The motion for a new trial in the alternative should be granted for the following reasons:

1. The verdict was contrary to law;

2. The verdict was contrary to the evidence;
3. The verdict was contrary to the law and the evidence;
4. The Court erred in refusing to direct a verdict for the defendant;
5. There was no evidence that, at the time of the accident referred to in the complaint, the tractor described in the policy referred to in the complaint was being used for the transportation of merchandise;
6. The verdict was contrary to the weight of the evidence;
7. The trial Court erred in refusing to give defendant's proposed instruction No. 3;
8. The trial Court erred in refusing to give defendant's proposed instruction No. 5;
9. The trial Court erred in refusing to give defendant's proposed instruction No. 7;
10. The trial Court erred in refusing to give defendant's proposed instruction No. 8;
11. The trial Court erred in refusing to give defendant's proposed instruction No. 9;
12. The trial Court erred in refusing to give defendant's [33] proposed instruction No. 10;
13. The trial Court erred in giving plaintiffs' proposed instruction No. 10;
14. The trial Court erred in giving plaintiffs' proposed instruction No. 11, as modified;

15. The trial Court erred in giving plaintiffs' proposed instruction No. 12, as modified;

16. The trial Court committed error in refusing to set aside the order striking (1) those portions of defendant's answer commencing on page 5, line 10 and ending with the word "them" on page 10, line 17 of said answer, and (2) that portion of said answer beginning on page 10, line 18, entitled "As to Second Alleged Cause of Action" which refers to and incorporates by reference those portions of said answer referred to in clause (1) hereof.

Wherefore, the defendant prays that the verdict of the jury herein, and the judgment rendered and entered thereon, be set aside, and that a judgment be rendered and entered herein in favor of the defendant; and the defendant further prays in the alternative that the Court set aside said verdict and judgment on behalf of the plaintiffs and grant the defendant a new trial herein, and that the Court so condition its order granting such new trial that the same shall become effective only in the event that such judgment notwithstanding the verdict shall be reversed on appeal.

LEIGHTON M. BLEDSOE,
DANA, BLEDSOE & SMITH,
Attorneys for Defendant. [34]

STIPULATION

It is stipulated that the foregoing motions may be heard on Monday, July 12, 1948, at ten o'clock a.m. of said day, before the Hon. L. R. Yankwich,

Judge of said Court, in the courtroom of said Court in which said Judge may be sitting, in the Post Office Building at San Francisco, California.

/s/ NATHAN G. GRAY,

Attorney for Plaintiffs.

/s/ LEIGHTON M. BLEDSOE,

/s/ DANA, BLEDSOE & SMITH,

Attorneys for Defendant.

[Endorsed]: Filed July 12, 1948.

[35]

[Title of District Court and Cause.]

DECISION AND ORDER

Upon the ground stated in the opinion filed herewith, the various motions heretofore argued and submitted are now decided as follows:

I.

The motion of the defendant for a directed verdict, on which ruling has been reserved, is granted.

II.

The verdict and judgment for the plaintiff is set aside and the Clerk of the Court is directed to enter judgment for the defendant that plaintiffs take nothing by their Complaint against the defendant.

III.

The motion for a new trial is denied.

Costs to the defendant.

Dated this 26th day of July, 1948.

LEON R. YANKWICH,

U. S. District Judge.

[Endorsed]: Filed July 26, 1948.

[36]

District Court of the United States, Northern
District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Monday, the 26th day of July, in the year of our Lord one thousand nine hundred and forty-eight.

Present: the Honorable Leon R. Yankwich, District Judge.

[Title of Cause.]

**MOTION FOR A DIRECTED VERDICT
GRANTED, MOTION FOR A NEW TRIAL
DENIED**

The motion of defendant for a directed verdict upon which ruling was reserved, and the motion of defendant for a new trial heretofore having been submitted for consideration and decision, and consideration having been had, it is Ordered that the motion for a directed verdict be and the same is hereby granted, and that the motion for new trial be and the same is hereby denied, as will appear more fully in an opinion and decision filed this date. [37]

[Title of District Court and Cause.]

OPINION

Appearances: For the Plaintiffs: Nathan G. Gray, Esq., Berkeley, California. For the Defendant: Robert Cathcart, Esq. and Dana, Bledsoe & Smith, San Francisco, California. [38]

Yankwich, District Judge:

I.

THE RESERVED MOTION FOR DIRECTED VERDICT THE DEFENDANT'S ALTERNATIVE MOTIONS

The plaintiffs, by their action, sought to recover from the defendant a total of \$5,118.76, with interest, alleged to be due on a judgment secured by them on September 16, 1947, in the Superior Court of the State of California, in and for the City and County of San Francisco, against Allen J. Warner and Robert W. Woodrow.

Warner and Woodrow were co-partners engaged in the transportation of property for hire, as a business, over public highways in the State of California, by means of motor vehicles. They had been authorized by the Railroad Commission of California to operate such business, and obtained a permit, as required by the law of California. (1) When the permit was issued, Warner and Woodrow were required by the Commission to secure a policy of public liability. The policy was issued by the defendant on April 19, 1946, and was in effect on June 22, 1946, when the accident for which the

recovery had been had in the Superior Court action had occurred. The defendant, having refused to pay the judgment, this action was instituted. A motion for a directed verdict, made by the defendant at the close of the plaintiff's case, was denied. At the conclusion of all the evidence, the defendant again moved for a directed verdict. Action on the motion was reserved. (2) The jury returned a verdict in favor [39] of the plaintiffs. The defendant has moved for a judgment notwithstanding the verdict, or, in the alternative, for a new trial.

II.

THE DECISIVE QUESTION

Under the interpretation which the Supreme Court has placed on Rule 50(b), we are required to rule on both motions. (3) The decision to be arrived at depends on our answer to one question:

Was the accident and the consequent injury to the plaintiffs, for which they recovered, in the Superior Court of the State of California, the judgment sued on here, within the terms of the public liability policy issued by the defendant?

And the answer is conditioned on the meaning of Declaration No. 5 in the policy, which reads:

“The automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation:”

Compliance with the statutory insurance requirement is a condition precedent to the granting of a

permit by the California Railroad Commission. (4)

Under the Insurance Code of California, the common carrier liability insurance includes insurance against any loss

“from liability of a common carrier for accident or injury fatal or non-fatal to any person.” (5)

And, while such liability includes any loss for which the peril insured against was the proximate cause, it excludes [40]

“any liability for a loss for which the peril insured against was only a remote cause.” (6)

The collision between the truck owned by the defendant and the automobile of the plaintiffs, which resulted in injury to them, occurred in Humboldt County, California, at a distance of three miles from the town of Scotia, Humboldt County, on Public Highway 101. Warner, one of the partners in the trucking business, is our sole source of information as to the circumstance under which he found himself on June 22, 1946, with the truck, without the trailer, at the place where the accident occurred. His story is contradictory. The version he gave on the first day of the trial as to the object of his trip from San Francisco differs from that which he told at the trial in the Superior Court, and at a hearing in this court in an action for declaratory judgment, to which he was made a party, and in which a declaration of non-coverage was secured against him and his co-partner. (7)

In both of those proceedings, he insisted that the trip from San Francisco, where his business is

located, to a small lumber town and resort thirty miles south of Eureka, where his sister resides, was purely a pleasure trip. He took his mother and his wife to see his sister, and to vacation. At the trial here, he claimed that the trip combined both business and pleasure. The business feature of the trip lay in the fact that he carried some 750 feet of pipe and some furniture [41] and stoves for his sister, for which she paid him \$75.00. After his arrival in Humboldt County, he remained nearly a week, during which he assisted in the building of a water line, leaving the work to be finished by more expert mechanics. He returned to San Francisco, a distance of some 250 miles, on June 22, 1946, leaving behind the trailer, which weighs 5 tons, and has a capacity of 15 tons. There was still some pipe on it, and some of the goods which he had brought up. In fact, on his second trip to San Francisco, he took back a large stove which his sister could not use. His wife accompanied him on the return trip. And the sole object of the trip was to pay a premium on the liability policy here involved, which was due June 22, 1946, and which he claims he paid with the cash into which he converted the travelers' checks in the sum of \$75.00, which his sister had paid him for transporting the pipe and the household goods.

After the motion for a directed verdict had been made at the conclusion of all the testimony, Warner was recalled for the purpose of amplifying the version given the day before, and particularly, the

statement that in returning to San Francisco, he also had in mind soliciting trucking business from a contractor residing at San Jose—a Mr. Dowdell. So, on the second day of the trial, he added that he had in mind soliciting from Dowdell and another contractor for whom he had transported materials, but that, as a fact, he did not do so after reaching San Francisco. On the contrary, after paying the premium, he [42] started back for Humboldt County, where he picked up the trailer and returned to San Francisco once more.

We are confronted here with the inherent improbability of a story, which bears almost on the fantastic. Motivation appears in the fact, admitted by Warner on the stand, that he made no mention whatever of the transportation of the pipe when he reported the accident to the highway patrol officer who interviewed him at the scene, or to the agent of the defendant, to whom he gave a full statement of the incident, which was reduced to writing and signed by him. In these statements, made shortly after the accident, the aim of the trip was given as a vacation for his mother, wife, and himself. He claimed that the reason for the omission of the fact that he was carrying the pipe and the household goods was that he thought it unimportant. He admitted, however, that he began to think about the possible significance of the transportation feature of the trip, when, in talking to other truck operators, they reminded him that this transportation might have a bearing upon the liability insur-

ance which he carried. One fact stands out in this narrative: The main purpose of the return trip was made to pay the premium. This main purpose was, in fact, the sole purpose, because we cannot consider any intention not carried into effect, such as solicitation of business.

III.

THE LAW APPLICABLE

It is to be borne in mind that we are interpreting [43] a contract which contains a condition or limitation of liability, regardless of whom has the burden of the proof. (8) Liability does not attach unless the truck, whether alone or with the trailer attached, was actually being used in the transportation of merchandise for hire. And when the facts are not disputed—whether the truck was, at the time of the accident, engaged in the sole activity covered by the policy is a question of law for the court. (9)

In interpreting exceptions or limitations of the type here involved, courts have adopted a latitudinarian rule of construction. And, if it appear that a vehicle covered by the policy, while not strictly used in the acts to which the exception limited it, was being used in the doing of of something which, either under the terms of the policy, or under a broad rule of construction, could be considered “incidental” to the main activity, courts will not hesitate to find liability. Illustrative are the following:

When a policy covered a vehicle operated as a "jitney bus", the fact that, at the time of the accident, it was on a different route than the route to which it was limited by municipal ordinance does not affect liability. (10)

Insurance of an automobile while used in the business of "auto tours" applied to the return trip to a passenger's home, when, by reason of bad weather, the trip to the real estate development was cancelled. (11) [44]

Liability has also been found when there was deviation from the route of a truck (12), where a tractor and trailer were standing empty on the highway after they broke down and their cargo was removed (13), when the vehicle turned into a garage or shop for repair (14), and when a motor bus, after arriving at its terminal, traversed the streets of a city for the purposed of being gassed or parked (15).

Behind all these cases runs the norm that if the vehicle, at the time of the accident, can be said to be on a mission incident to the object to which its use is limited, the courts will give full effect to the policy.

However, if the vehicle is doing something totally unrelated to the use or the physical incident which resulted in the accident is not contemplated by the policy, liability does not exist. Thus, indemnity insurance on vehicles used "incidental to business of funeral director" does not include use of an automobile to transport, for hire, a wedding party. (16)

A "collision" does not include the turning over of the automobile on the edge of a road without striking or colliding with another object other than the ground (17), or the striking of the road with the body of the automobile when the front axle broke. (18)

A policy of insurance indemnifying against risk incident to the hauling of coal with trucks does not cover the use of a truck by one of the insured's employees for pleasure, after working hours. (19)

The reason back of these cases has been stated in this language:

"While it is true that insurance contracts should be construed most strongly against the insurer (*French v. Fidelity & Casualty Co.*, 135 Wis. 259, 115 N.W. 869, 17 L.R.A. (N.S.) 1011; *Kelly v. Fidelity Mut. L. Ins. Co.*, 169 Wis. 274, 172 N.W. 152, 4 A.L.R. 845), yet they are subject to the same rules of construction applied to the language of any other contract. It is a fundamental rule that the language of a contract is to be accorded its popular and usual significance. It is not permissible to impute an unusual meaning to the language of any other contract. The incident causing the damage to the automobile here in question is spoken of in common parlance as an upset or tip-over. If it were the purpose to insure against damage resulting from such an incident, why should not such words, or words of similar import, have been used? We cannot

presume that the parties to the contract intended that an upset should be construed as a collision in the absence of a closer association of the two incidents in popular understanding.” (20) (Emphasis added)

It is evident from a consideration of these cases that the use of a portion of the insured equipment, the truck part, to return to the place of origin, San Francisco, 250 miles away, [46] not for the purpose of picking up a new load, or beginning a new haul, or storing or repairing the truck, but for the purpose of paying a premium on an insurance policy on the truck, is not an act incidental to the transportation of goods on the truck or trailer. Nor, for that matter, is the soliciting of business an incidence of such transportation. To be accessory to the business in which the truck was used, it would have to be covered by a policy which, either did not include any limitation, or insured generally against any act or acts of the defendant while engaged in trucking for hire. But the policy here under consideration was not so comprehensive. The defendant did not insure against all the risks of the plaintiffs while engaged in the business of trucking, but only against a specific risk. Otherwise put, it insured the automobiles when

“used only for transportation of merchandise purposes.” (Emphasis added)

The Railroad Commission rider attached to the policy, which is reproduced in the margin, did not

enlarge on the coverage. (21) Its aim, as I stated at the argument, was to protect the public against certain defenses arising from violations of the law by employees, lack of authorized use and the like, which might defeat liability. It did not, and could not, change a coverage limited to a specific use to a general coverage of the truck, regardless of the use. And, insofar as any of the cases outside of the Ninth Circuit or of California (22), hold to the contrary, they do not require assent. For, aside from the fact [47] that in the face of a conflict of authorities, we may choose those which seem to us the more logical, the case before us, being a diversity case, is controlled by state law. (23)

Rejecting an identical contention as to the effect of an obligatory rider imposed by a Kansas statute, the Circuit Court of Appeals for the Tenth Circuit said:

“Defendants argue that the effect of the rider required by the Corporation Commission was to make plaintiff liable under the policy for damage resulting while the truck was operated for pleasure, notwithstanding that such loss was expressly excluded from coverage.

They construe that part of the rider stating that no violation of any of the provisions of the policy by the insured should relieve the company from liability thereunder to mean that the company would be liable for any damage suffered by the insured, whether resulting

while the truck was being operated in his business of a contract carrier or outside of such business.

“The only power the Corporation Commission has is to adopt rules that will effectuate the statute. It may not adopt any regulation changing the statutory liability. *Dunn v. Jones*, 143 Kan. 218, 53 P. 2d 918. No doubt the Legislature could have required as a prerequisite to the issuance of a permit that the applicant therefor file an indemnity policy protecting the public against all loss resulting [48] from the operation of the truck, whether operated in the business of a contract carrier or for pleasure, or otherwise. * * * The policy did not include coverage for loss from operations other than those of a contract carrier, nor did the permit require such coverage. The damage admittedly was incurred while the insured was operating the truck for pleasure and outside the coverage of the policy. Plaintiff was not liable to respondent in damages for the loss suffered by defendants while the truck was being operated other than in the business of assured a a common carrier.” (24) (Emphasis added)

Cases which seem to declare a contrary ruling are distinguishable on the facts. The courts found, either in the policies themselves, or in the statute under which they were issued, an intention not to limit the use of the vehicle to distinct operations.

This was the situation in *Smith v. California Highway Indem. Exchange*. We quote from the opinion:

“* * * Davis was operating his jitney bus on the ‘29th and Mission’ route, which extended from the ferry at the foot of Maket Street to Valencia Street, thence to Twenty-ninth and Mission. He resided at 311 Jersy Street, which is about five blocks from [49] Twenty-ninth and Mission Streets. On the afternoon of the accident he had returned to his home for the purpose of taking a rest, in preparation for his night run. He parked his car in front of his home, on a grade. After his rest, he entered his car, released the brake and backed down grade to the corner of Noe Street, where he struck the plaintiff.

“* * * It cannot be doubted that the Chandler automobile was ‘maintained’ by Davis for the purpose and business of a jitney bus at the time of the accident. It was operated at the time ‘in the service of the subscriber as a jitney bus . . . within the city and county limits of the city of San Francisco’, and it may not fairly be said that the car was at the time operated for any other purpose than that of a jitney bus. Necessarily Davis was required to keep the car somewhere and it was kept at his home which was the place specified in his operator’s permit where it was to be kept and

which was in the vicinity of the Twenty-ninth and Mission terminus of the route. At the time of the accident, he was operating, using and maintaining his car with the equipment, plates and badge placed and displayed as required by local regulations. The policy did not specify the particular or any route over which the car should be operated. [50] The limits of the operation thereof were the city and county of San Francisco." (Emphasis added)

It is thus evidence that a return trip must be related directly to the business in which the vehicle is to engage, or to the specific act of transportation, if the policy is so limited. And this was the case here. The trip on which the accident occurred was not a use within the terms of the policy.

IV.

CONCLUSION

From what precedes, it follows that the motion for a directed verdict, on which ruling has been reserved, should be granted, the verdict and judgment for the plaintiffs set aside and judgment for the defendant entered. (26)

This conclusion still calls for the disposition of the motion for a new trial. (27)

I realize that this motion could be granted conditioned on its taking effect only if the judgment notwithstanding the verdict is reversed on appeal.

(28)

However, in this case, the motion for a new trial

should be denied. Obviously, if my interpretation of the insurance policy is correct, the jury's verdict is wrong.

If the jury's verdict is right, it can only be because the case presented a factual situation for their solution.

If this be so, then—despite what is said in this opinion about the unsatisfactory character of the testimony [51] concerning the nature of the trip on which the accident occurred—I should allow the jury's conclusion upon the facts to stand and not substitute my own for it. (29)

The motion for a new trial will, therefore, be denied.

Dated this 26th day of July, 1948.

LEON R. YANKWICH,
United States District Judge.

NOTES TO TEXT

1. California Highway Carriers Act, Sections 1, (c) (f), 3; Dearing's General Laws, Act 5129 (a), Secs. 1 (c) (f), 3.

2. Federal Rules of Civil Procedure, Rule 50 (b); See, *Dickerson v. Franklin Nat. Ins. Co.*; 1942, 4 Cir., 130 F (2) 35; *Western Union Telegraph Co. v. Dismang*, 1939, 10 Cir., 106 F (2) 362, 363-364; *Howard v. Swagart*, 1947, U. S. App. D. C., 161 F (2) 651, 655; *Cone v. West Virginia Pulp & Paper Co.*, 1947, 330 U. S. 212; *Fratta v. Grace Line, Inc.*, 1943, 2 Cir., 139 F(2) 743.

3. *Montgomery Ward & Co. v. Duncan*, 1940, 311 U. S. 243.

4. The Highway Carriers Act, Secs. 5, 6 & 7; Deering's General Laws, Act 5129 (a), Secs. 5, 6 & 7.

5. California Insurance Code, Sec. 110.

6. California Insurance Code, Sec. 530.

7. The action for declaratory judgment was instituted by the defendant in this case for the purpose of securing a declaration of non-liability. The plaintiffs here were named parties defendant, summons directed to them was issued, but they were not served. Warner defaulted. After a hearing before the Honorable Louis E. Goodman, one of the Judges of this court, a judgment was entered on August 14, 1947, decreeing that the accident was not covered by the policy. A similar judgment was entered on October 27, 1947, against the co-partner, Robert W. Woodrow, after his default. The defendant in this case pleaded this judgment as res judicata. The portion of the Answer which stated this plea [53] was stricken, on motion, by the Honorable Michael J. Roche, on March 1, 1948. At the trial, the defendant sought to restore this defense, but I declined to do so, agreeing with the view of Judge Roche that the judgment was binding only on the parties who were served with process and appeared or defaulted, and not on the plaintiffs, who, although made parties, were not served, and did not appear. The case cited by the defendant, *Bernhard v. Bank of America*, 1942, 19 C (2) 807, 811-813, does not go counter to these rulings. It recognizes the principle which limits the binding effect of a judgment to parties and their privies.

The plaintiffs here were not represented in that action by the defaulting partners. There was no identity of persons or of cause of action, under such circumstances as result in estoppel by judgment. See, 50 C.J.S., Judgments, Secs. 601, 648, 768; and see, *Tait v. Western Maryland Ry Co.*, 1933, 289 U. S. 620, 623; *Hardy v. Rosenthal*, 1934, 2 C. A. (2) 442, 444-446; *Sasser v. First Joint Stock Land Bank*, 1938, 5 Cir., 99 F (2) 744, 745; *Rheinberger v. Security Life Ins. Co.*, 1945, 7 Cir., 146 F (2) 680, 683.

8. See, *Zohner v. Sierra Nev. L. & Co.*, 1931, 114 C. A. 85, 90; *Cardoza v. West Am. Comm. Ins. Co.*, 1935, 6 C. A. (2) 500, 502; *Ellis v. Order of United Commercial Travelers, etc.*, 1942, 20 C (2) 290, 304.

9. *Universal Automobile Ind. Co. v. Noel*, 1933, 9 Cir., 64 F (2) 916; *Moblad v. Western Indemnity etc. Co.*, 1921, 53 C. A. 683; *Sumida v. Pacific Automobile Ins. Co.*, 1942, 53 [54] C. A. (2) 472.

10. *Smith v. California Highway Indemnity Exchange*, 1933, 218 Cal. 325.

11. *Davis v. California Indemnity Exchange*, 1931, 118 C. A. 403.

12. *Central Mutual Ins. Co. v. Tartar*, 1937, 6 Cir., 92 F (2) 839.

3. *Liberty Mutual Ins. Co. v. McDonough*, 1938, 6 Cir., 97 F (2) 497.

14. *Mitchell v. Great Western State*, 1942, 140 Ohio St. 137, 42 N. E. (2) 771, 141 A. 624.

15. *American Fidelity & C. Co. v. McWilliams*,

1937, 55 Ga. App. 658, 191 S. E. 191; and see, *Johnson Transfer & Freight Lines v. American National Ins. Co.*, 1935, 168 Tenn. 514, 79 S. W. (2) 587; *Selber v. Commonwealth Casualty Co.*, 1930, 106 N. J. L. 611, 150 A. 243.

16. *Heritier v. Central Indemnity Co.*, 1942, 109 N. J. L. 313, 162 A. 573.

17. *Moblad v. Western Indemnity Co.*, 1921, 53 C. A. 683. See also, *Bell v. American Ins. Co.*, 1921, 173 Wis. 533, 181 N. W. 733; *Flythe v. Eastern Caroline Coach Co.*, 1928, 195 N. C. 777, 143 S. E. 865.

18. *Bell v. American Insurance Co.*, *supra*.

19. *Gudbransen v. Peltó*, 1939, 205 Minn. 607, 287 N. W. 116.

20. *Bell v. American Insurance Co.*, *supra*, at p. 734. The language just quoted was adopted by the California District Court of Appeals in *Moblad v. Western Indemnity Co.*, *supra*, a case which, in turn, has the approval of the Circuit Court of Appeals for the Ninth Circuit. See, *New Jersey Ins. Co. [55] v. Young*, 1923, 9 Cir., 290 Fed. 155.

21. "The policy to which this endorsement is attached is an Automobile Bodily Injury Liability and Property Damage Liability policy, and is hereby amended to assure compliance by the insured, as a motor carrier of property, with appropriate provisions of law (Highway Carriers' Act, Statutes 1935, Chapter 223, as amended; City Carriers' Act, Statutes 1935, Chapter 312, as amended; and Public Utilities Act, Statutes 1915, Chapter 91, as amended); and with the pertinent rules, orders,

and regulations of the Railroad Commission of the State of California.

“In consideration of the premium provided for in the policy of which this endorsement is made a part the Company agrees that within the classes of coverage provided by the policy it will pay any final judgment rendered against the insured for bodily injuries to or death of any person or persons other than the named insured, or damage to or destruction of property, or both, arising out of the ownership, maintenance or use of any vehicle operated under authority of the aforesaid statutes, although such vehicle may not be specifically described in the policy; that the judgment creditor may maintain an action in any court of competent jurisdiction to compel such payment; that the right of any person, firm or corporation to recover under the policy shall not be affected by any act, omission, or misrepresentation of the insured or his employees with regard to any warranty, condition, declaration, or provision of the policy; and that the policy shall remain in full force and effect notwithstanding such act, omission or misrepresentation or the violation of any warranty, condition, declaration or provision of the policy by the insured or his employees; Provided, However, that this endorsement shall not be construed [56] to impose any obligation on the Company for which it would not be liable independently hereof with respect to (1) bodily injuries to or death of employees of the named insured arising out of or in the course of their employment, (2) bodily injuries

to or death of any person occurring while such person is riding in or upon or entering or alighting from any vehicle covered by the policy, (3) loss of or damage to property owned by, rented to, in charge of, or transported by the insured, or (4) any loss arising out of any operations of the insured except operations authorized or for which authorization is required under the aforesaid statutes. The insured agrees to reimburse the Company for any payment made by the Company on account of any accident, claim, or suit involving a breach of the terms of the policy, and for any payment that the Company would not have been obligated to make under the provisions of the policy, except for the agreement contained in this endorsement.

“The Company further agrees that such insurance as is afforded by the policy and this endorsement against liability for injuries to or death of persons and damage to or destruction of property shall not be cancelled, rescinded, or suspended, nor shall the cancellation, rescission, or suspension of the policy or of this endorsement take effect, nor shall the policy or this endorsement become void for any reason whatsoever, except by the expiration of the term for which it is written, until the Company shall have first given ten days’ notice in writing to the Railroad Commission of the State of California at its offices, State Building, [57] San Francisco, California. Said ten days’ notice shall commence from the date notice is received at said office of said Commission.

“The Company further agrees that if the policy

shall be cancelled or suspended or otherwise terminated, and shall thereafter be reinstated, notice in writing of such reinstatement shall immediately be given by the Company to said Commission at its said office.

“The Company further agrees that this endorsement shall prevail over any conflicting provision in the policy or in any other endorsement now or hereafter attached thereto or made a part thereof; Provided, However, that this endorsement shall be of no effect with respect to any liability in excess of \$5,000 for bodily injuries to or death of any one person and \$10,000 for bodily injuries to or death of two or more persons in any one accident, and \$5,000 for damage to or destruction of property of one or more than one claimant in any one accident.

“Nothing in this endorsement shall be construed to limit or restrict any coverage otherwise provided by the policy of which this endorsement is made a part.

“When countersigned by an authorized representative of the Company this endorsement becomes a part of Policy No. MC 170330 issued by Commercial Standard Insurance Company (herein called Company) of Fort Worth, Texas, to Allen J. Warner and Robert W. Woodrow, effective April 19, 1946. Countersigned at San Francisco this 19th day of April, 1946.

By E. L. MITCHELL,
Authorized Company Representative.” [58]

22. *Travelers Mutual Casualty Co. v. Thornsbury*, 1936, 276 Ky. 762, 125 S. W. (2) 229; *Rusch v. Mielke*, 1940, 234 Wis. 380, 291 N. W. 300.

23. *Angel v. Bullington*, 1947, 330 U. S. 183, 186-187. See also, *King v. Order of Travelers*, 1948, 333 U. S. 153, 157-158.

24. *Foster v. Commercial Standard Ins. Co.*, 1941, 10 Cir., 121 F (2) 117, 119. And see, *Smith v. Republic Underwriters etc.*, 1940, 152 Kan. 305, 103 P (2) 858, 860; *Hawkeye Casualty Co. v. Halferty*, 1942, 8 Cir., 131 F (2) 294; *Associated Indemnity Co. v. Bunney*, 1942, 9 Cir., 137 F (2) 1, in which our own Circuit Court of Appeals approves *Foster v. Commercial Standard Ins. Co.*, *supra*; *Simon v. American Casualty Co.*, 1944, 4 Cir., 146 F (2) 208; *Stewart v. Hoffmeister*, 1932, 16 Tenn. App. 495, 65 S. W. (2) 220, 224-226. The following statement from *Smith v. Republic Underwriters*, *supra*, at p. 860, sums up the position here taken:

“There is nothing novel in the limitation of coverage contained in the instant endorsement. For instance, provisions are common which limit coverage to specified use of the vehicle. In fact, the instant provision is really one as to use. * * * To disregard this limitation in the policy or to hold it invalid would constitute an attempt to expand the insurer's liability, and if accepted by the insurance carrier, an increase in premiums would inevitably result.” (Emphasis in text.) [59]

25. 218 Cal. 325, 326-327.

26. Federal Rules of Civil Procedure, Rule 50 (b).

27. *Montgomery Ward & Co. v. Duncan*, 1940, 311 U. S. 243.

28. *Western Union Telegraph Co. v. Dismang*, 1939, 10 Cir., 106 F (2) 362; 363-364; *Howard v. Swagart*, 1947, U. S. App. D. C., 161 F (2) 651, 656; *McIlvaine Patent Corporation v. Walgreen Co.*, 1943, 7 Cir., 138 F (2) 177, 179-180;

29. *Aetna Casualty & Surety Co. v. Yeatts*, 1941, 4 Cir., 122 F (2) 350, 352-354; *Murphy v. United States District Court*, 1945, 9 Cir., 122 F (2) 1018, 1020. And see my opinion in *Caldwell v. Southern Pacific Co.*, 1947, D. C. Calif., 71 Fed. Sup. 955, 962-963.

[Endorsed]: Filed July 26, 1948.

[60]

In the District Court of the United States, North-
ern District of California, Southern Division

No. 27,857-R

GEORGE W. BOULTER and
MARGARETTA L. BOULTER,

Plaintiffs,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant.

JUDGMENT

The above-entitled action came on regularly for trial on July 6, 1948 before the Court sitting with a jury, Nathan G. Gray appearing as counsel for the plaintiffs and Dana, Bledsoe & Smith (by Robert Cathcart of counsel) appearing as counsel for the defendant. At the close of all of the evidence, the defendant having moved the Court for a directed verdict in its favor and the Court having reserved its ruling on said motion, the jury returned a verdict in favor of plaintiffs and against defendant in the total amount of Five Thousand One Hundred Eighteen Dollars and Seventy-six Cents (\$5,118.76), with interest thereon; judgment having been entered on said verdict on July 9, 1948, and the defendant having thereafter renewed its motion for a directed verdict and having, in addition, moved the Court for Judgment in its

favor notwithstanding the verdict and, in the [61] alternative, for a new trial, and said motions having been taken under advisement, and the Court having on July 26, 1948, filed herein its Decision and Order (supported by the Court's written opinion) granting defendant's motion for a directed verdict and granting defendant's motion for judgment in its favor notwithstanding the verdict, and ordering said verdict and judgment for the plaintiffs set aside, and directing the Clerk of the Court to enter Judgment for the defendant that plaintiffs take nothing by their Complaint against the defendant, and denying defendant's motion for a new trial in the alternative.

It Is, Therefore, Ordered, Adjudged and Decreed that defendant's motion for a directed verdict be, and the same is hereby, granted; that defendant's motion for judgment in its favor notwithstanding the verdict be, and the same is hereby, granted; that the verdict for the plaintiffs and judgment thereon heretofore entered be, and the same are hereby, set aside;

It Is Further Ordered, Adjudged and Decreed that plaintiffs take nothing by their Complaint against defendant, that the Complaint be dismissed on the merits, and that defendant recover from plaintiffs its costs, in the amount of \$....., as taxed, and that defendant have execution thereon.

It Is Further Ordered, Adjudged and Decreed that the Clerk insert in this Judgment the amount

of the costs, as taxed, and that the Clerk enter this Judgment of record.

Dated this 5th day of August, 1948.

LEON R. YANKWICH,
Judge of the United States District Court.

[Endorsed]: Vol. 5, Page 84. Filed Aug. 5, 1948.

Entered in Civil Docket Aug. 6, 1948. [62]

[Title of District Court and Cause.]

NOTICE OF APPEAL TO THE UNITED
STATES CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

Notice Is Hereby Given that the plaintiffs above named, George W. Boulter and Margretta L. Boulter, do, and each does, hereby appeal to the United States Circuit Court of Appeals for the Ninth Circuit from:

1. That certain decision and order made by and filed in the record of this court on the 26th day of July, 1948, granting the motion of the defendant for directed verdict on which ruling had been reserved, and setting aside the verdict and judgment for the plaintiffs and ordering the clerk of this court to enter judgment for the defendant that plaintiffs take nothing by their complaint against the defendant; and

2. From the final judgment entered of record in the office of the clerk of the above entitled court on the 6th day of August, 1948, in favor of the

defendant above named, and against the plaintiffs above named. [63]

Said appeal is taken from the whole and each and every part of said decision and order, and from the whole and every part of said final judgment.

/s/ NATHAN G. GRAY,
Attorney for Appellants, George W. Boulter and
Margretta L. Boulter.

[Endorsed]: Filed Aug. 18, 1948.

[64]

[Title of District Court and Cause.]

DESIGNATION OF THE PORTIONS OF THE
RECORD, PROCEEDINGS, AND EVIDENCE
TO BE CONTAINED IN THE RECORD
ON APPEAL

Notice Is Hereby Given that the plaintiffs and appellants, George W. Boulter and Margretta L. Boulter, do hereby designate the following portions of the record, proceedings, and evidence to be contained in the record on appeal in this cause:

1. Complaint.
2. Answer of Defendant to Complaint.
3. Demand for Trial by Jury.
4. Request for Admission of Facts.
5. Statement of Defendant Commercial Standard Insurance Company in Reply to Plaintiffs' Request for Admission of Facts.
6. All evidence received during the trial, includ-

ing the testimony of all witnesses, all stipulations or admissions of counsel, all writings and other exhibits received in evidence, all motions and applications made during the trial and the rulings thereon. [65]

7. The verdict of the Jury and Judgment entered thereon.

8. Motion of Defendant for Judgment Notwithstanding the Verdict and in the Alternative for a New Trial.

9. Minute order granting motion of defendant for judgment notwithstanding the verdict.

10. Decision and Order filed on July 26, 1948.

11. Opinion of the trial court.

12. Judgment entered pursuant to said decision and order.

13. Notice of Appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

14. Designation of the Portions of the Record, Proceedings, and Evidence to be Contained in the Record on Appeal.

15. All other records required by the provisions of Rule 75, Subdivision (g), of the Federal Rules of Civil Procedure.

/s/ NATHAN G. GRAY,

Attorney for Appellants, George W. Boulter and
Margretta L. Boulter.

(Affidavit of Service by Mail.)

[Endorsed]: Filed Aug. 18, 1948.

[66]

[Title of District Court and Cause.]

STATEMENT OF POINTS UPON WHICH
THE PLAINTIFFS AND APPELLANTS
INTEND TO RELY ON THE APPEAL IN
THIS CAUSE

1. The allegations of the complaint were all proven without conflict or admitted by the pleadings or stipulation.

2. The plaintiffs established a prima facie case entitling them to recover as prayed for in their complaint.

3. The court committed error in granting the motion of the defendant for a directed verdict in that plaintiffs established a prima facie case and the granting of said motion was based on the testimony of Allen J. Warner, a witness called by defendant.

4. The testimony of the witness, Allen J. Warner, was discredited, and the jury had a right to disregard all or any part of his testimony.

5. The court usurped the function of the jury in directing a verdict for the defendant and entering judgment in favor of defendant notwithstanding the verdict of the jury in favor of the plaintiffs.

6. The evidence was sufficient to sustain the verdict of the jury in favor of the plaintiffs.

/s/ NATHAN G. GRAY,
Attorney for Appellants, George W. Boulter and
Margretta L. Boulter.

(Affidavit of Service by Mail.)

[Endorsed]: Filed Aug. 23, 1948.

[68]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR FILING
RECORD ON APPEAL

Good cause appearing therefor, It Is Hereby Ordered that the time for filing and docketing the record on appeal in the above entitled cause be, and the same is hereby, extended to and including the 15th day of October, 1948.

Dated September 17th, 1948.

MICHAEL J. ROCHE,
Judge of said U. S. District Court.

[Endorsed]: Filed Sept. 17, 1948. [69]

District Court of the United States
Northern District of California

CERTIFICATE OF CLERK

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify the foregoing 69 pages, numbered 1 to 69, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of George W. Boulter and Margretta L. Boulter, Plaintiffs, vs. Commercial Standard Insurance Company, a corporation, Defendant, No. 27857-R, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of \$9.40 and that the said amount

has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 5th day of October, A. D. 1948.

(Seal)

C. W. CALBREATH,
Clerk.

[70]

[Title of District Court and Cause.]

REPORTER'S TRANSCRIPT

Tuesday, July 6, 1948

Appearances: For the Plaintiffs: Nathan G. Gray, Esq. For the Defendant: Robert Cathcart, Esq.

(A jury was duly impanelled and sworn to try the case.)

(Mr. Nathan G. Gray then made an opening statement to the jury.) [1*]

NOEL COLEMAN,

called as a witness on behalf of the plaintiff; sworn.

The Clerk: Will you state your name to the Court and the jury? A. Noel Coleman.

Direct Examination

By Mr. Gray:

Mr. Gray: Q. Mr. Coleman, will you state your business or office?

* Page numbering appearing at foot of page of original certified Reporter's Transcript.

(Testimony of Noel Coleman.)

A. Yes, sir, I am assistant secretary of the California Public Utilities Commission.

Q. And how long have you had that position?

A. Since February, 1946.

Q. Now the Public Utilities Commission was formerly the Railroad Commission, was it?

A. That's correct.

Q. And when was the name changed from the Railroad Commission to the Public Utilities Commission?

A. It was changed by Constitutional amendment on November 1, 1946. [2]

Q. So when we refer to "Railroad Commission" in the past, or "Public Utilities Commission" now, we are referring to one and the same thing, is that right?

A. That's correct.

Q. All right. Now Mr. Coleman, you have the records of permits issued under the Highway Carriers Act, you have some of the records with you?

A. Yes, sir, I have.

Q. And do you have any record of an application for a permit and a permit that was issued to Allan J. Warner and Robert W. Woodrow?

A. Yes, sir, I have.

Q. And would you state with reference to June, 1946, when was the last time prior to that date that they applied for a permit under the Highway Carriers Act?

A. They were given a Highway Common Carrier permit numbered 38-3486 under date of June 28, 1945.

(Testimony of Noel Coleman.)

Q. And that permit remained in effect how long? A. Until December 1, 1946.

Q. And as far as your records are concerned, it was in full force and effect on June 22, 1946, was that right? A. That's correct.

Q. Now as a condition for granting this permit, does your Commission require that Warner and Woodrow obtain a policy of insurance? [3]

A. Yes, sir.

Q. And was such a policy of insurance obtained? A. Yes, sir.

Q. And you have in your files a certificate certifying that such was issued?

A. Yes, sir. It is covered by policy number MC170330, effective from April 19, 1946, to April 19, 1947.

Q. And that policy to which you just referred—

Mr. Gray: Counsel, will you stipulate that is the policy here involved?

Mr. Catheart: I am sure it is, if you say it is, Mr. Gray.

Mr. Gray: I believe it is.

The Court: Very well.

Mr. Gray: Q. Is it permissible for you to remove any of those documents? A. No, sir, it is not.

Q. You have to keep it intact?

A. I have to keep them intact, yes, sir.

The Court: Now what is it you are taking out of this?

Mr. Gray: I think it probably has it in the certificate, your Honor—

(Testimony of Noel Coleman.)

The Court: I think you can read the substance of it into the record. Is any issue made, gentlemen, about these preliminary steps under the policy?

Mr. Cathcart: No, as far as I know, your Honor. [4]

Mr. Gray: In other words, counsel, do you stipulate that at the time of this action and for a time prior thereto and subsequent thereto, the policy that we have referred to in the complaint was in full force and effect, subject to whatever the terms of the policy are?

Mr. Cathcart: Well the policy was in full force and effect subject to its terms. I do not stipulate that at the time of this action it was in effect. That is why we are here.

Mr. Gray: I am not asking you to stipulate on the coverage.

The Court: No, you are not stipulating coverage, but that the coverage, according to the terms to be shown, was in effect.

Mr. Cathcart: Surely.

Mr. Gray: Well, putting it another way, counsel, in your other action for declaratory relief, you attached a copy of the policy.

Mr. Cathcart: Yes.

Mr. Gray: To that action, to your complaint.

Mr. Cathcart: Yes.

Mr. Gray: Will you stipulate that that complaint had attached to it a true copy of the policy here involved? Or do you have the original policy?

(Testimony of Noel Coleman.)

Mr. Cathcart: We have already covered all this in your [5] demand and our answer, and we have admitted that to be the fact.

Mr. Gray: Well, do you have the original policy here?

The Court: Well, a copy, gentlemen, is attached here.

Mr. Gray: Well that policy that the defendant attached in his action, your Honor, I don't believe the defendant did it intentionally, but the insurance company neglected to attach the endorsement that we feel is very important.

The Court: I see.

Mr. Gray: I am sure they didn't do it intentionally.

Mr. Cathcart: I just referred to it by reference; it was a Railroad Commission write-up. Here is the original policy in this other action. I wonder if we could have it removed from the other action file.

The Court: Well, we won't remove it, but we can take it by reference as an exhibit.

Mr. Cathcart: Surely.

Mr. Gray: All right, then, counsel has handed me the file in action number 26544-G, Civil, in this Court, entitled Commercial Standard Insurance Company, a Corporation, vs. George W. Boulter and Margretta L. Boulter, Allan J. Warner, Robert Woodrow, and certain fictitious parties. And is it stipulated, counsel, that in this file is the original policy and is the document right here?

(Testimony of Noel Coleman.)

Mr. Cathcart: Yes, that is my understanding, Mr. Gray. [6]

Mr. Gray: And that is that.

Mr. Cathcart: This is the Railroad Commission rider, right here.

Mr. Gray: All right. And it is stipulated that subject to the terms of the policy, whatever they are, it was in full force and effect at all times on June 22, 1946?

Mr. Cathcart: Subject to the terms of the policy.

Mr. Gray: Subject to the terms of the policy, it was in full force and effect?

Mr. Cathcart: Well it was issued before that date and it was in effect at a date subsequent to that date. Now I don't want you to think I am quibbling about whether it was in full force and effect, but the policy was outstanding. It is just that it is still a question.

The Court: Well gentlemen, you are talking about different things. You were talking coverage.

Mr. Cathcart: That's right.

The Court: And he is talking about the existence of the policy.

Mr. Cathcart: That's correct, your Honor.

Mr. Gray: You accept my stipulation?

Mr. Cathcart: Surely.

The Court: All right.

Mr. Gray: Then if the Court please, may this policy to which I have just referred, and this is a policy— [7]

The Court: Let me ask you—. Just a moment, I want to ask the Clerk about some customs.

(Testimony of Noel Coleman.)

(A conversation was had between the Clerk and the Court out of the hearing of the Reporter.)

The Court: All right, go ahead. I always like to consult the local Clerk as to the customs, whether they could be removed. In our district they don't allow removal, so we take it by reference. The Clerk will mark it by reference, and then of course you can read any portion of it that you desire to the jury at the proper time.

Mr. Gray: Certainly.

The Court: All right.

Mr. Gray: Then at this time, your Honor, the plaintiffs offer in evidence a policy of insurance on the stationery of Commercial Standard Insurance Company, bearing the number MC170330, which purports to have been issued on April 19, 1946, and to expire on April 19, 1947. I will ask that this policy be admitted.

The Court: It may be so marked and received by reference.

Mr. Gray: Thank you.

The Clerk: Plaintiff's Exhibit No. 1.

(Insurance Policy No. 170330, Commercial Standard Insurance Company, referred to above, was received in evidence as Plaintiff's Exhibit No. 1, by reference.)

[Printer's Note: Plaintiff's Exhibit No. 1 is printed out in full as Exhibit "B," page 25 of

(Testimony of Noel Coleman)

this printed record, with following added rider attached to Plaintiff's Exhibit No. 1:]

(Supersedes all endorsements heretofore required by said Commission)

The policy to which this endorsement is attached is an Automobile Bodily Injury Liability and Property Damage Liability policy, and is hereby amended to assure compliance by the insured, as a motor carrier of property, with appropriate provisions of law (Highway Carriers' Act, Statutes 1935, Chapter 223, as amended; City Carrier's Act, Statutes 1935, Chapter 312, as amended; and Public Utilities Act, Statutes 1915, Chapter 91, amended); and with the pertinent rules, orders, and regulations of the Railroad Commission of the State of California.

In consideration of the premium provided for in the Policy of which this endorsement is made a part the Company agrees that within the classes of coverage provided by the policy it will pay any final judgment rendered against the insured for bodily injuries to or death of any person or persons other than the named insured, or damage to or destruction of property, or both, arising out of the ownership, maintenance or use of any vehicle operated under authority of the aforesaid statutes, although such vehicle may not be specifically described in the policy; that the judgment creditor may maintain an action in any court of competent jurisdiction to compel such payment; that the right

(Testimony of Noel Coleman)

of any person, firm or corporation to recover under the policy shall not be affected by any act, omission, or misrepresentation of the insured or his employees with regard to any warranty, condition, declaration, or provision of the policy; and that the policy shall remain in full force and effect notwithstanding such act, omission or misrepresentation or the violation of any warranty, condition, declaration or provision of the policy by the insured or his employees; Provided, However, that this endorsement shall not be construed to impose any obligation on the Company for which it would not be liable independently hereof with respect to (1) bodily injuries to or death of employees of the named insured arising out of or in the course of their employment, (2) bodily injuries to or death of any person occurring while such person is riding in or upon or entering or alighting from any vehicle covered by the policy, (3) loss of or damage to property owned by, rented to, in charge of, or transported by the insured, or (4) any loss arising out of any operations of the insured except operations authorized or for which authorization is required under the aforesaid statutes. The insured agrees to reimburse the Company for any payment made by the Company on account of any accident, claim, or suit involving a breach of the terms of the policy, and for any payment that the Company would not have been obligated to make under the provisions of the policy, except for the agreement contained in this endorsement.

(Testimony of Noel Coleman)

The Company further agrees that such insurance as is afforded by the policy and this endorsement against liability for injuries to or death of persons and damage to or destruction of property shall not be cancelled, rescinded, or suspended, nor shall the cancellation, rescission, or suspension of the policy or of this endorsement take effect, nor shall the policy or this endorsement become void for any reason whatsoever, except by the expiration of the term for which it is written, until the Company shall have first given ten days' notice in writing to the Railroad Commission of the State of California at its office, State Building, San Francisco, California. Said ten days' notice shall commence from the date notice is received at said office of said Commission.

The Company further agrees that if the policy shall be cancelled or suspended or otherwise terminated, and shall thereafter be reinstated, notice in writing of such reinstatement shall immediately be given by the Company to said Commission at its said office.

The Company further agrees that this endorsement shall prevail over any conflicting provision in the policy or in any other endorsement now or hereafter attached thereto or made a part thereof; Provided, However, that this endorsement shall be of no effect with respect to any liability in excess of \$5,000 for bodily injuries to or death of any one person and \$10,000 for bodily injuries to or death

(Testimony of Noel Coleman)

of two or more persons in any one accident, and \$5,000 for damage to or destruction of property of one or more than one claimant in any one accident.

Nothing in this endorsement shall be construed to limit or restrict any coverage otherwise provided by the policy of which this endorsement is made a part.

When countersigned by an authorized representative of the Company this endorsement becomes a part of Policy No. MC 170330 issued by Commercial Standard Insurance Company (herein called Company) of Fort Worth, Texas, to Allen J. Warner and Robert W. Woodrow, effective April 19, 1946, 12:01 a.m., standard time at the address of the insured as stated in said policy.

Countersigned at San Francisco this 19th day of April, 1946.

By /s/ E. L. MITCHELL,
Authorized Company Representative.

The Court: In due time, ladies and gentlemen, the counsel [8] will read the portions they desire to be read in order to have any records transcribed that are prepared in this case.

Mr. Gray: Q. Well, Mr. Coleman, from your standpoint, from the standpoint of your Commission, then, the permit was issued in reliance of this policy, of which you had a certificate in your files, is that correct?

(Testimony of Noel Coleman.)

A. We had a certificate in our files.

Q. And on June 22, 1946, at all times on that day as far as your records are concerned, Warner and Woodrow had a permit to engage in the business of transporting merchandise for hire, is that correct?

A. As far as our records are concerned, yes sir.

Mr. Gray: Thank you. That is all.

The Court: Any questions, Mr. Cathcart?

Cross-Examination

By Mr. Cathcart:

Mr. Cathcart: Q. Mr. Coleman, your records of course do not show the activities of Warner and Woodrow from day to day, as they operated their business? A. No, sir, they do not.

Q. So that when you speak of this policy being in effect, you mean that your records do not show that there were any existing defenses to it or that the people named therein were engaged in something other than transportation of merchandise?

A. Not that we know of.

Mr. Cathcart: Yes. Thank you.

The Court: All right.

The Witness: May I be excused?

The Court: The witness is excused.

(Witness excused.)

The Court: All right, call your next witness.

Mr. Gray: Now if the Court please, we have entered into a stipulation to the effect that I may state in open Court, and this will be regarded as evidence in this case,—

The Court: Yes.

Mr. Gray: —that the judgment that Mr. and Mrs. Boulter obtained in a State court has never been paid. No part of that judgment has ever been paid, and the whole of it is now due, owing and unpaid.

The Court: And the amount is \$3,000 for Mr.—?

Mr. Gray: Well, the amount is alleged in the complaint. I will give it to your Honor. As to George W. Boulter, the amount is \$3,000 with interest at 7% from and after the 16th of September, 1947, which we have not computed. To the plaintiff Margretta L. Boulter, it is the sum of \$2,000 with interest of 7% from the 16th of September, 1947, and for both defendants, is the sum of \$118.76, costs incurred.

The Court: I see. All right. That is the unpaid portion of the judgment. [10]

* * * *

Mr. Gray: The plaintiff rests, your Honor.

The Court: All right. [11]

* * * *

Afternoon Session, Tuesday, July 6, 1948

2:00 o'clock p.m.

The Court: All right, let the record show that the following proceedings are had outside the presence of the jury.

I was informed that you had a motion to make, and rather than bring in the jury and then excuse them, I thought I would give you greater freedom by having them remain out until the motion is concluded.

Mr. Cathcart: Thank you, your Honor. At this time the defendant moves for a dismissal of this action under the provisions of rule 41-b; on the ground that the plaintiff, after completing the presentation of his evidence, has not shown any right to relief.

Now our position is substantially this: The plaintiff has put in evidence an insurance policy which on its face provides that the automobile described is and will be used, only for transportation of merchandise purposes, and will be operated as follows—and this insurance covers for no other use or operation.

Now it is our position that, although certain special defenses may place on us the burden of at least going ahead on the defense, on the fundamental proposition of whether or not there is coverage to this particular incident, we submit [13] that the burden is on the plaintiff. Now if I were suing on a fire policy and all I showed was that my house had been destroyed, I think that I would have to show that it had been destroyed by fire. Similarly, in any action between the assured, and of course the third party who has recovered the judgment here is in no better position than the assured—it would be up to the assured to show that it falls perfectly within the four corners of the policy; not

as to the conditions subsequent, not as to the failure to give notice, special defenses of that kind. I concede that if this were that type of a defense on the policy, the burden of showing one of those special defenses would be ours. But to bring us into Court, I submit that in this case it was up to the plaintiffs to prove that at the time of the accident the defendant, or rather the assured, was engaged in the transportation of merchandise. I submit on that point. [14]

* * * *

The Court: I may say, gentlemen, that since we adjourned, I have studied the cases that you called to my attention, and the question in each case, and I gather from the cases I read, is as to whether the condition that is alleged was violated is a condition precedent to recovery or not. I think, Mr. Cathcart, the case that you cite, the Ellis case, the mutual benefit case, is the typical double indemnity clause, which states that a person can recover if the death occurs by accidental means.

* * * *

So I feel that in this case a prima facie case has been shown when they produce a judgment of the Court in addition to the other facts, which shows a recovery against them for injury caused by their truck and the conditions of liability are general and imposed by statute; the limitation becomes an exception, which it is duty of the defendants to prove.

Now I don't want to deprive you of the right to make any further comments; I just wanted to tell

you my reaction on the case you cited and the other cases, and why, in my opinion, regardless of the fact that there are now all sorts of limitations, which have been placed by our Circuit Court of Appeals on the right to direct a verdict and also to dismiss a matter upon a motion at the close of the plaintiff's testimony—

Mr. Cathcart: Well, we must submit the motion without any further argument, your Honor.

The Court: Very well. What do you call your motion, a motion to dismiss or a motion for a directed verdict?

Mr. Cathcart: A motion to dismiss.

The Court: All right, the motion will be denied.

Mr. Cathcart: Well, at this time—

The Court: You have some instructions? [19]

Mr. Cathcart: At this time we request a directed verdict.

The Court: A directed verdict?

Mr. Cathcart: I should like to move for a directed verdict at the conclusion of the evidence, which will be put in this afternoon.

The Court: Well you have a right to move under the rules both times, either at the conclusion of the plaintiff's case or at the conclusion of both.

Mr. Cathcart: Yes.

The Court: And as we have to inform you of the actions on instructions before the argument—which is the rule now which obtains on both the civil and criminal cases, you will have ample opportunity to do so. I usually excuse the jury, so that you will have ample opportunity, when the evi-

dence is concluded and before the argument to make such motion in addition to the form of instructions which you have submitted.

Mr. Cathcart: Surely. Now there are a couple of other points that I would like to take up at this time very briefly in order to protect ourselves on the record here.

In this case we pleaded *res adjudicata*, alleging in our answer that the fact of non-coverage had been determined in an action for declaratory relief brought by the insurance company, the defendant in this action, against the assured, Warner and his partner, and also against the Boulters, the [20] plaintiffs in this action. We were unable to effect this service on the Boulters. We obtained a judgment on a hearing. It was a default judgment. It was made on a hearing before Judge Goodman, and now Judge Roche ordered that defense stricken on the ground that it was not *res judicata*, for the reason presumably that the Boulters were not a party to that action. We had argued that since the action of the plaintiffs was derivative, their rights were no larger than those of the assured, and that a judgment against the assured would bar the plaintiffs in this action.

So at this time again, just to protect our record, I ask that the order striking the second ground of defense, specifically, paragraphs 6 and 7—I beg your pardon, paragraph 7 of our answer, be vacated and set aside and on it being granted, I offer to prove the granting of the declaratory judgment by Judge Goodman, in which it was declared that the

insurance policy which is the subject matter of the present action did not cover the accident involved in this case.

The Court: All right.

Mr. Cathcart: And I submit that motion. Well, I say that I submit the motion—I am making, of course, an offer of proof to prove the existence of a judgment. [21]

* * * *

The Court: The motion will be denied.

Mr. Cathcart: And there is one other point I would like to bring up at this time, your Honor. Since we now have the duty of going ahead with the proof, it is obvious that the assured, Warner, is the man whose evidence will be necessary [24] to us. Now I suggest that we should be permitted to examine him as an adverse witness. Of course if we are to be bound by everything he says, he will probably say that he is insured, which is a very normal reaction. Accordingly, I submit that we should be permitted to examine him as an adverse witness, and not be bound.

The Court: I don't see how you can, under Section 43-c. I haven't the rules before me.

Mr. Cathcart: It says that if he is hostile or adverse, he may be led.

The Court: Well, he isn't proved to be adverse. You have to prove that he is hostile. You have to show by regular rules. You can't call him under Section 43-b because he is not an adverse party. And to interrogate an unwilling or hostile witness, you must first show that he is hostile. If you know

in advance that he is going to be hostile, you can't call him.

* * * *

[25]

The Court: I cannot determine that in advance, you will have to call him, and then after you call him, if you lay a foundation in a proper manner, why then I will rule upon the [27] question.

* * * *

ALLAN J. WARNER,

called on behalf of the defendant, sworn.

The Clerk: Will you state your name?

A. Allan J. Warner.

Direct Examination

By Mr. Cathcart:

Q. Mr. Warner, in what place do you live?

A. I live at Number 10 Ord Court.

Q. And how long have you lived there?

A. 27 years.

Q. I see. And are you in business of some kind?

A. I was.

Q. At the present time, or not?

A. No, I am not.

Q. I see. And there has been reference here to an accident that involved a certain piece of equipment—that was brought up. I will ask you if on June 22, 1946, you were in business.

A. Yes, sir, I was.

Q. And were you by yourself or were you with someone? A. I was in partnership.

Q. And what was your partner's name?

A. Robert W. Woodrow.

(Testimony of Allan J. Warner.)

Q. And at that time did you engage—well, what kind of business was it?

A. Transportation of property for hire.

Q. I see. And what kind of equipment did you have?

A. I had a 1939 Dodge with a 1938 trailer, a tractor and trailer.

Q. I beg your pardon?

A. Tractor and trailer.

Q. A tractor-trailer combination?

A. That's right.

Q. Now just what is that tractor? Just try to describe it. What sort of an instrument is it?

A. Well, a tractor is a truck without a body on it. It has got a fifth wheel on it.

Q. What is that fifth wheel? [29]

A. The fifth wheel supports the weight of the trailer. In other words, well, it is a tractor-trailer combination, that's all.

Q. I see. Well, now, describe briefly the trailer.

A. The trailer was a 1937 or 1938—I don't remember now— Stake trailed. It was a 24 foot trailer, I believe.

Q. The trailer was 24 feet long?

A. I believe so.

Q. You say a stake trailer, you mean it had stakes up on the sides? A. That's right.

Q. Now going back to the tractor again, what is it used for, what is the use made of a tractor?

A. The tractor pulls the trailer.

(Testimony of Allan J. Warner.)

Q. The tractor pulls the trailer; and does that tractor have any kind of a body on it?

A. It has got a plate, well, this particular one.

Q. It has? That is the one I am talking about.

A. Well, we are talking about this particular one. This particular one had a pair of saddle tanks on it. Across the saddle strappings was a plate.

Q. What is that plate made of? A. Steel.

Q. I see. Now what is the purpose of that plate?

A. Well that plate is, as a general rule, for carrying axles [30] and lines, and cables, chain, gear.

Q. Gear for use in connection with the truck, is that it? A. Yes, more or less.

Q. I see. And now is there any kind of cab on this truck, or this tractor?

A. Yes, it has got a conventional cab on it.

Q. I see. And how many places are there in the cab? A. How many—what do you mean?

Q. Well I mean, can two people sit there?

A. Yes, two people could sit there—three could sit there.

Q. I see. And at this particular time, where was your place of business?

A. I operated out of Number 10 Ord Court, my home.

Q. That is in San Francisco, is it?

A. Yes, sir.

Q. I see. And where were your operations generally, in the six months before that time? Was there any definite route you would follow?

(Testimony of Allan J. Warner.)

A. No, no definite route. I wildecatted.

Q. I see. Well where did you go while you wildecatted?

A. Well I used to run to San Jose regularly and Sacramento, I used to go as far as Stockton, all around this locality.

Q. I see. And have you told us now about most of the places you used to go to while you were wildecatting?

A. Yes, as far as I can remember. [31]

Q. What does "wildecatting" mean?

A. Well, a wildecat is one that has no definite over-the-road operation of his own, so he sub-hauls for big contractors.

Q. I see. Did you follow the practice of sub-hauling for these contractors? A. I did.

Q. Who were some of those big contractors in particular? A. One of them was—

Mr. Gray: Just a moment, I object on the ground that it is incompetent, irrelevant, and immaterial.

The Court: Yes, I will sustain the objection.

Mr. Cathcart: Q. And now do you recall having been involved in an accident with any of the equipment on June 22, 1946?

A. You mean this particular piece of equipment?

Q. Yes. A. Yes, I do.

Q. Well now you say this particular piece of equipment; what particular piece of equipment do you mean?

(Testimony of Allan J. Warner.)

A. The 1939 tractor, the Dodge tractor.

Q. The Dodge tractor? A. Yes.

Q. And where was that accident?

A. I think it was about two miles south of Scotia.

Mr. Cathcart: Now just to get some of these points a little clearer, with your Honor's permission and Mr. Gray's [32] permission, I am going to ask to have introduced in evidence a Shell road map just so that this gentleman can refer to it and we can tell where this thing happened.

Mr. Gray: Well if your Honor please, I don't quite understand the purpose of it. The accident is not being tried. I think as long as we agree there was an accident and that we got the judgment, that is all that matters. I don't quite see the materiality. Maybe I am missing something.

The Court: Well, I think the place where the accident occurred is material in view of the defense that is raised.

Mr. Gray: All right.

The Court: All right.

Mr. Cathcart: I am not advertising for the Shell Oil Company, but this is useful as a map; may I show it to the witness?

The Court: All right. What county is this in? The town of Scotia—what county is that in?

Mr. Cathcart: Scotia is a few miles south of Eureka.

The Court: Is it Humboldt County?

Mr. Cathcart: It is Humboldt County, yes sir.

(Testimony of Allan J. Warner.)

The Court: All right.

Mr. Catheart: Q. Now is that the Scotia you have reference to? (Indicating) A. Uh-huh.

Q. I see. Now at the time that that accident happened, in which [33] direction were you going?

A. I was coming South.

Q. And where was the trailer at that time?

A. The trailer was in Eureka, or to be exact, Blue Lakes.

Q. Well now, Blue Lakes — which particular Blue Lake was that?

A. Well that is what they call the south fork of Willow Creek.

Q. Is that near Eureka?

A. Yes, it is 34 miles this side of Eureka.

Q. It is not this Blue Lakes up here in Lake County, I take it? A. No.

Q. And is that Blue Lake between the scene of the accident and Eureka, just so that the jury can have it in their minds as to where this thing happened? A. No, not exactly.

Q. Well where was it with reference to Eureka, are they both south of Eureka?

A. Southeast of Eureka.

Q. I see. Now at the time that this accident happened, were you alone?

A. No sir, I wasn't.

Q. Who was with you? A. My wife.

Q. And what was your destination?

A. I was coming back to San Francisco. [34]

Q. When had you gone to Blue Lakes?

(Testimony of Allan J. Warner.)

A. A week prior to that.

Q. And on that trip a week prior to that, what was your point of departure?

A. San Francisco.

Q. And were you driving the tractor at that time? A. Yes I was.

Q. Did you have the trailer with you at that time? A. Yes I did.

Q. This was a week prior to the accident, now, is that correct? A. That's right.

Q. And what was your destination at that time?

A. The south fork of Willow Creek.

Q. And was there anything in the trailer at that time? A. Yes, I had 700 feet of pipe.

Q. And where were you taking that pipe to?

A. To Willow Creek.

Q. Who owned the pipe? A. My sister.

Q. Were you carrying it at her request?

A. Yes I was.

Q. Did she pay you for it? A. She did.

Q. All right. Now how long did it take you to get from San Francisco to Willow Creek, if you remember? [35]

A. About nine hours, I guess.

Q. And what did you do when you got to Willow Creek?

A. Well with this pipe I had a load of furniture, too.

Q. Yes. Now tell us about that too.

A. Well that was on the same deal.

(Testimony of Allan J. Warner.)

The Court: Whose furniture was that, was that hers too?

The Witness: My sister's too.

The Court: Well all right, tell us what you did with any equipment that you carried after you got there.

A. Well, she had bought a place up there on the south fork of Willow Creek, and I left the pipe there. I put in a water system for her up there with the pipe. I left the furniture there. Now there was an outfit in Eureka, I think it is in Eureka, but it is up there near Eureka, maybe Korbelt—I forget which it is. There was a big barrel place up there.

The Court: Well, go ahead. What did you do?

The Witness: Well it had been my intentions to get a load out of there back for San Francisco. As a general rule, you try to load both ways. Or, a load of lumber or something else—anything coming out. Well, right at the time there was nothing coming out of that particular territory.

The Court: All right.

The Witness: (Continuing) So I headed back for San Francisco with the tractor. [36]

Mr. Cathcart: Q. Did you leave your trailer up at Willow Creek? A. Yes I did.

Q. Now what time did you leave Willow Creek on the morning that this accident happened?

A. I left Willow Creek at about 5 o'clock, I guess, in the morning.

Q. I see. About what time did the accident hap-

(Testimony of Allan J. Warner.)

pen? A. I would say about 1 o'clock.

Q. In the afternoon? A. Yes.

Q. And was that between Willow Creek and San Francisco that that accident happened?

A. That was between Scotia and San Francisco that it happened.

Q. I see. And is Willow Creek north of Scotia?

A. Yes it is.

Q. On Highway 101, is it?

A. Well no, it is off of 101, it is on a county road.

Q. I see. Well as you came from Willow Creek to Highway 101, where did you hit Highway 101?

A. About 16 miles from 101 on the county road.

Q. Well, I mean on what point on 101 did you hit 101? A. I don't follow you.

Q. Well visualize yourself on the county road.

A. Yes. [37]

Q. You are trying to get to San Francisco. You have told us that you came to Highway 101, is that correct? A. That's correct.

Q. Now where did you come to Highway 101?

A. From a little place called, I think it is Korbel. It is a little lumber town.

Q. But is that on Highway 101?

A. No, it is not on Highway 101, it is on the county road.

Q. Well where do you come into 101? In Eureka? A. Yes, I believe so.

Q. I see. So is this correct, that you left this

(Testimony of Allan J. Warner.)

little place at Willow Creek and drove to Eureka and then went south on Highway 101?

A. Yes, I believe so.

Q. Well, I don't want to mislead you or misquote you. I just want to get what the facts are.

A. Will you repeat it for me?

The Court: Mr. Reporter, would you read the question, please?

(Record read.)

A. That's right.

Mr. Cathcart: Q. And do you recall offhand how far south of Eureka Scotia is?

A. No I don't.

Q. Had you driven that area before? [38]

A. I had been up there a few years before then.

Q. You have relatives up there, do you?

A. No sir.

Q. Was this at the time of any vacation that you had? A. Yes, it was.

Q. And had you spent some of the vacation up there?

A. At the same time I took the lumber up and the pipe and the furniture, I spent my vacation there too.

Q. I see. And this that you talked about doing, for whom was that done?

A. For my sister, my older sister.

Q. She lives up there, does she?

A. Yes, she does.

(Testimony of Allan J. Warner.)

Q. Well I meant by your family, any of your relatives—do some of them live up there?

A. No, she is the only one.

Q. I see. Now you told us that you went up there with your trailer loaded with furniture and pipe and other things—where was the trailer at the time of the accident?

A. At the time of the accident?

Q. Yes. A. The trailer was in Eureka.

Q. I see. And had you left it there?

A. I had left it there.

Q. You had unloaded it. Had you unloaded the pipe and the [39] furniture? A. I had.

Q. And about how long before the accident would it be that the trailer had been unloaded?

A. How long before the accident?

Q. Yes, how many days, if you know.

A. No, not before the accident.

Q. Well I misunderstood you now. Was the trailer still loaded at the time of the accident?

A. The trailer was being unloaded the morning I left.

Q. I see. And it was being unloaded in Eureka?

A. No, at Willow Creek.

Q. At Willow Creek. That is, as you left at 5 a.m., 5 o'clock in the morning, you saw them unloading the trailer?

A. They were finishing unloading my trailer, yes sir.

Q. Now what was your purpose in going to San Francisco?

(Testimony of Allan J. Warner.)

A. There was an installment due on the policy, this policy. It was due on a Monday morning, or it was due, anyway— I forget how many hours I had grace, but that was my reason for coming to San Francisco as I did, without the trailer.

Q. And did you arrive in San Francisco?

A. I did.

Q. Did you make the run from Eureka to San Francisco without the trailer? A. I did.

Q. And did this accident happen on that run?

A. Yes.

Q. When I say "this accident", I mean the accident in which Mr. George Boulter and Mrs. Margretta Boulter received these injuries that we have been talking about. A. That's right.

Q. And on this trip in which you had been going north carrying the load to your sister-in-law, did you say? A. Yes, my sister.

Q. Sister. I beg your pardon. Were there any bills of lading on that trip or anything of that kind?

A. I don't believe there was. It isn't—

Q. Go ahead, I beg your pardon.

A. It is not a common procedure to turn out a bill of lading for a wildcat load.

Q. I see.

The Court: Q. Well you were doing nothing but wildcat load on the whole?

A. That's right.

Q. How would you handle the situation?

A. Well that, there is a notation made of it,

(Testimony of Allan J. Warner.)

and that is to pay my Board of Equalization and California Railroad Commission; there is a notation made, and then it is kept and put aside or entered in the books.

Q. Who enters the notation, you yourself, or someone else on the books? [41]

A. No, my partner, as a general rule.

Q. On books you keep for that purpose?

A. On books we keep for the California Railroad Commission and the Board of Equalization.

The Court: All right.

Mr. Cathcart: Q. On this particular occasion, did you make any entry for this trip for your sister?

A. That I don't know right now for sure.

Q. You mentioned something about some operations in the Willow Creek area. What sort of operations did you mean? A. You see—

Q. Soliciting business, I mean?

A. Soliciting business, exactly.

Q. And did you see anybody up at Willow Creek in connection with that? A. Yes I did.

Q. You did? A. I did.

Q. When was that?

A. That was the morning, I think—let's see, that was on a Sunday morning. I seen the foreman of the lumber company there.

Q. Which particular Sunday morning was that?

A. Well that was the morning, the Sunday morning before the Monday morning that I left for San Francisco.

(Testimony of Allan J. Warner.)

Q. You left up there on Monday morning? [42]

A. Or Saturday morning. I don't know when. It is a long time ago now.

Q. Well whom did you see up there, do you recall?

A. Well, it has been a long time, and that was the first time I had ever been up there. I don't know anybody up there, so I wouldn't know just exactly who it was.

The Court: Well what business were they in?

The Witness: Lumbering.

The Court: Q. The lumber business?

The Witness: There was, or I believe there still is, several backwoods lumber companies up there.

Q. Do they have yards in the little towns?

A. In Eureka.

Q. I see.

A. And at Berkeley, across the Bay, I believe some of the lumber from up in that territory comes down as far as Berkeley. Some of it goes down as far as San Jose.

The Court: All right.

Mr. Cathcart: Q. Well did you have a conversation with this person that you were talking about?

A. Yes, I believe I did.

Q. And you don't recall his name or the names of his company?

A. He didn't tell me his name. He merely asked me if I was interested in hauling lumber out of the valley from the valley floor up there into Eureka and I told him that I was. [43]

(Testimony of Allan J. Warner.)

Q. I see. Now—

The Court: Well, let's follow that up.

Q. What was the status of that negotiation?

A. Of the lumber deal?

Q. At the time you left, yes.

A. Well there was several things that—

Q. Well did he give you any promise, did you get any promise?

A. Well, you see the mill was just opening up.

Q. The main point is this; did you make a deal, did he promise to give you something to carry back?

A. No, the mill wasn't in a position to board lumber yet, it was merely that if I would come back up there in a couple of weeks, when the mill was in a position to run, well, that I would be able to pull the machinery and stuff like that out of Berkeley and lumber back out of Eureka, back to San Francisco.

The Court: All right, go ahead.

Mr. Cathcart: Q. Did you return to Eureka?

A. You mean after the accident?

Q. Yes. A. I did.

Q. How soon?

A. I think it was Wednesday, on a Wednesday.

Q. Now this accident happened on your way to San Francisco, is that correct? [44]

A. That's right.

Q. And after the accident you continued on to San Francisco, is that correct?

A. That's correct.

Q. And how many days did you stay in San Francisco?

(Testimony of Allan J. Warner.)

A. I was in until, I went down to the insurance company and notified the insurance company on Monday morning of the accident, and I paid my premium. That was on a Monday morning. Tuesday morning—Wednesday morning I left for Eureka, back up again. I had had the truck repaired Monday, the tractor rather, here in town. I went back up again to get my trailer.

Q. And do you recall the day when you arrived back in Eureka? A. No, I don't.

Q. Where was your trailer when you arrived back up there?

A. Well my trailer was sitting on my sister's property.

Q. That would be at Willow Creek?

A. That was at Willow Creek.

Q. I see. And then what did you do?

A. Then I came back to San Francisco.

The Court: Q. Well did you pick up your trailer? And the pipes then unloaded from your trailer?

A. Everything had been unloaded. I had a haul at the time with John Dowdell, of San Jose. That is John Dowdell, Draymen; I believe we were hauling concrete pipe out of San Jose for housing projects all over the area, the peninsula area. [45] That was one of the—

Q. Well the point is this; you came back empty?

A. Yes.

Q. You just went back to get the trailer?

A. No, I got my trailer and—

(Testimony of Allan J. Warner.)

Q. By the way, when you came back the first time, when you came to San Francisco, was your wife with you? A. My wife was with me.

Q. When did she come back—was she with you at the time of the accident?

A. She was with me at the time of the accident.

Q. Well did you leave her behind when you went back again? A. Yes I did.

Q. You went back alone? A. Yes.

Q. And you went back to get the trailer?

A. That's right.

Q. And the only reason you came back to San Francisco instead of waiting until the pipe was unloaded was because you wanted to return back and pay this premium?

A. To pay my premium, yes sir.

Q. I see.

The Court: All right, go ahead.

Mr. Cathcart: Q. Now do you know how many days that trailer was at Willow Creek before it was unloaded? [46]

A. No, I don't. I have no idea.

Q. Well you delivered it there, didn't you?

A. I did.

Q. To your sister-in-law's property?

A. That's right.

Q. You parked it in your sister-in-law's property? A. That's right.

Q. Were you visiting her?

A. I was visiting, with my principal reason, as I said, being the pipe. I installed a water system for her up there while I was there.

(Testimony of Allan J. Warner.)

Q. You started right away to do that, did you?

A. I did.

Q. And when did you unload the pipe?

A. I finished unloading it, or they finished unloading it, I got the pipe all used up.

Q. Right away?

A. No, I think I worked on the pipe for about three days. This furniture was taken right off.

Q. The furniture was taken off as soon as you got there? A. That's right.

Q. And how about the pipe?

A. The pipe was: I used it; I took it off. As I was using it, I would take it off joint by joint.

The Court: Q. Did you use it all up? [47]

A. Yes, I did.

Q. I thought you said there was still stuff on that, that other people unloaded it for you?

A. No, there was a stove, a big Wedgewood stove and some other stuff that there was, no, they were not in a position to take this other stuff in right at the time.

Q. You mean your sister?

A. My sister. They had a little place up there; they had bought this place and it had nothing in it, and she would get the place in order for the stuff that they had then, then they would take it off the truck and put it into the house.

Q. Why didn't you leave it on the ground?

A. It is damp up there.

Q. Why didn't you leave the stuff on the ground and take your trailer back?

(Testimony of Allan J. Warner.)

A. Well there are several reasons for that. I don't know if you have ever been up north.

Q. Well the fact is I am not interested in that, I am asking you why you did what you did.

A. Well for me, with a 24 foot down off the mountain, it is difficult to get down to start with, I figured with a tractor, I could make better time. I figured with a tractor, like an automobile, a guy could make better time without pulling a heavy trailer. Which I did.

Q. In other words, you were intending to return back to San [48] Francisco, and your purpose was not just to return, but to hasten back to pay the premium on this policy?

A. To pay my policy.

Q. And then you were going to pick that up later? A. That is true.

The Court: I see. All right.

Mr. Cathcart: Q. Now you said that to make this trip to San Francisco, you could make better time in your tractor without that trailer hooked onto it. Just tell us about that. What do you mean by that?

A. Well that unit, that combination, I guess it is about 30 feet, and the roads up there in that section are fairly narrow. When you want to go around corners up there, you have to get out against the ravine, and it is difficult with a trailer.

Q. Well you could make better time with the tractor, is that correct? A. That's correct.

Q. And in fact, do you drive faster with a trac-

(Testimony of Allan J. Warner.)

tor when it is by itself than when the trailer is hooked on?

A. Not necessarily, not myself personally.

Q. I see. Now when from Willow Creek south to San Francisco for the purpose, as you tell us, of paying a premium on your insurance policy, were you transporting any merchandise?

A. No, I can't say that I was at the time.

Mr. Gray: If the Court please, I think probably to keep [49] the record clear, may that answer go out for a moment?

The Court: All right.

Mr. Gray: I would like to object to that as calling for the conclusion and opinion of the witness.

The Court: No, I don't believe so.

Mr. Gray: In other words, there is a distinction between carrying merchandise physically and in the legal sense; I am aware of the fact that physically he wasn't carrying merchandise.

The Court: Well, that is what he is asking for.

Mr. Gray: Well if that is what it is, I have no objection.

The Court: Well, ask it in a different manner.

Q. You weren't carrying anything coming home?

A. Coming home, no sir.

Q. In other words, you had no new load, and the load that you had brought up had either been used up, as in the case of the pipe, or it was still on the trailer when you left there?

A. Yes sir.

Q. I see. To be removed later on?

(Testimony of Allan J. Warner.)

A. Yes.

Q. I see. All right.

Mr. Cathcart: And now you told us that after you returned to Eureka, you picked up your trailer? A. Yes.

Q. How many days was that after you had returned to Eureka? [50]

A. That was on Wednesday. I paid my—

The Court: Premium?

The Witness: Yes. I paid my premium on Monday. Tuesday—or Monday afternoon, I went up and I had the truck gone over to get rid of the effects of the accident. Wednesday morning I left for Eureka again.

Q. Yes. You arrived back in Eureka on Wednesday?

A. I arrived back in Eureka about 12 o'clock, I think, Wednesday night.

Q. And your truck was where at that time, when you saw it? A. The trailer?

Q. Yes, I mean the trailer. I beg your pardon.

A. The trailer was where I had left it.

Q. At your sister-in-law's? A. Sister's.

Q. Sister's. I don't know why I keep making that mistake. Then when did you come back again?

A. Thursday morning.

Q. The very next Thursday morning or a week later?

A. No, that same Thursday morning.

Q. I see. And was your trailer loaded as you made that trip south?

(Testimony of Allan J. Warner.)

A. Well I had a big range and some other stuff coming back home.

Q. Who owned that range? [51]

A. It belonged to my sister too. I got \$64 bringing it back.

Q. And where did you deliver that?

A. I delivered that, to, I believe, my mother's place, at Number 10 Ord Court.

Q. I see. Then was it after that that this San Jose contract came up that you were telling us about?

A. That's right, the following morning, I believe that was a Friday morning. I left for Carmel.

Q. Yes. I see. Now did you get that contract after you got back to San Francisco?

A. I did.

The Court: Q. You didn't have that range going up, did you? A. Yes I did.

Q. She couldn't use it and sent it back?

A. She couldn't use it.

Q. Oh, I see. All right.

Mr. Cathcart: Q. When you took this—would you review this for me again a moment? When you took this cargo on your trailer up there—this is now before the accident happened—was your wife with you at that time?

A. My wife was with me.

Q. I see. And did she return the second time?

A. Back to Eureka?

Q. Yes. A. No, she didn't. [52]

(Testimony of Allan J. Warner.)

Q. I see. How much does the tractor and trailer weigh altogether, do you recall?

A. The tractor weighed $2\frac{1}{2}$ tons. The trailer weighed 3 tons, I believe. $5\frac{1}{2}$ tons.

Q. It was a $5\frac{1}{2}$ ton combination?

A. Approximately.

Q. I see.

Mr. Cathcart: I think that is all.

The Court: All right, you may cross-examine.

Cross Examination

By Mr. Gray:

Q. Mr. Warner, you were subpoenaed here to-day by me, is that right? A. I believe so.

Q. Yes. And in the action in the State court, you were represented, were you not, by Dana, Bledsoe and Smith, the lawyers for this insurance company, is that right? A. Yes I was.

Q. And then there was another proceeding which they had, these lawyers and this insurance company, with you, before Judge Goodman?

Mr. Cathcart: Now just a moment. If your Honor please, that is outside the issues in this case. We object to it on the ground that it is incompetent, irrelevant, and immaterial. [53]

The Court: Well, I think the relationship between the witness and counsel is material, as going to interest or bias or anything like that that counsel may wish to bring out.

Mr. Cathcart: Surely.

(Testimony of Allan J. Warner.)

The Court: We are not going into the lawsuit merely to show the lawsuit.

Mr. Cathcart: Well that was the only reason I was objecting.

Mr. Gray: That was the reason I was doing it, your Honor.

The Court: Very well, go ahead.

Mr. Gray: Q. Now Mr. Warner, when you were brought before Judge Goodman at the request of Mr. Bledsoe of this same law firm—is that correct? A. Yes sir.

Q. —and while you were before Judge Goodman, you gave certain testimony under oath, didn't you? A. Yes sir, I did.

Q. And in that hearing you were asked certain questions concerning the purpose of your trip up there to Willow Creek, is that right?

A. That's right.

Q. And I will ask you whether or not in that hearing before Judge Goodman, Mr. Bledsoe of this same law firm that represents the insurance company did not ask you certain questions.

The Court: I presume, counsel, if you have a transcript [54] of the testimony, counsel will probably stipulate that the questions were asked and answered.

Mr. Gray: Just a moment, your Honor, until I find the part I want.

Q. Now I will show you this transcript here. page 6, lines 3 to 12, and ask you whether these

(Testimony of Allan J. Warner.)

questions were asked of you and these answers were given before Judge Goodman.

Mr. Gray: Shall I read them, your Honor?

The Court: I beg your pardon?

Mr. Gray: May I read them?

The Court: No, I think the proper way is just to show them to him. If counsel will stipulate that he asked the questions and that the answers shown were given, I don't think you need read it.

Mr. Gray: Q. Would you read these that I have marked here? (Handing to witness.)

The Court: Don't read them out loud.

Mr. Gray: Just read them to yourself.

Mr. Cathcart: What is he reading, counsel?

Mr. Gray: He is reading on Page 6, lines 3 to 12.

Mr. Gray: Q. You have read those. I will ask you whether those questions were asked and those answers given by you? A. Yes, they were.

Mr. Gray: And if the Court please, they are as follows: [55]

"Mr. Bledsoe: Q. This trip was in the nature of a vacation trip for you, wasn't it?

"A. It was a combination.

"Q. What was the nature of the combination?

"A. Business had been very slow about that time of the year and we had gone up into Willow Creek for an outfit up there, California Barrel. We had intended, if possible, to haul barrels out of Willow Creek.

(Testimony of Allan J. Warner.)

“Q. Did you see someone while you were up there about that?

“A. No, I did not.”

Mr. Gray: Q. Now in this hearing before Judge Goodman, Mr. Warner, did you testify to anything about stoves, pipe, or furniture?

A. No, I didn't.

Q. Nothing was said about that?

A. (Witness nodded in the negative.)

Q. Now this tractor that is in your insurance policy is the same tractor as involved in this accident, is that right? A. That's right.

Q. Now were you paid for taking this pipe and other material up there? A. Yes sir, I was.

Q. How much were you paid? A. \$75.

The Court: Q. What size pipe was it?

A. One inch pipe.

Q. How much did you have, 750 feet?

A. I think it was 700 feet.

Q. How much did it weigh, do you know?

A. About, I should say for the whole load—I had about 6 ton.

Q. Including the stove?

A. Including the rest of the furniture, yes sir.

Q. All right. What capacity was the trailer?

A. Carrying capacity?

Q. Yes. A. Fifteen ton.

Q. That is the way it is registered, that amount?

A. I don't remember how it was registered now.

The Court: I see, all right.

Mr. Gray: Q. Now this accident occurred on

(Testimony of Allan J. Warner.)

Highway 101, is that right? A. I believe so.

Q. That is the redwood highway?

A. Yes.

Q. And at the time of this accident, were you taking the most direct route as far as you know from Willow Creek back to San Francisco?

A. Yes I was.

Q. Now you testified that the purpose in coming back was to pay [57] the premiums on the insurance policy. Is that the insurance policy here involved in this case? A. Yes.

Q. You were paying the premiums on that?

A. Yes sir.

Q. And you also testified that at the same time you notified the company of the accident?

A. Yes sir.

Q. And did you describe the accident to them at the time you notified them? A. I did.

Q. And did you give them the premiums at the same time? A. Yes sir, I did.

Q. They accepted the premiums?

A. They did.

Q. Well now let's see if we can get this straight about this trailer being unloaded up there. Was this trailer at the time you left Willow Creek loaded or unloaded?

A. The trailer was still partially loaded.

Q. Still partially loaded? A. Yes, sir.

Q. And you left it there for the purpose of being unloaded?

(Testimony of Allan J. Warner.)

A. Well not primarily to be unloaded, but so I could get out of there right then.

Q. All right. But was it your intention that the trailer be [58] unloaded at that time?

A. That's right.

Q. It was to be unloaded? A. Yes sir.

Q. And you intended to return for the trailer, is that correct? A. That's right.

Q. Now at the time—you testified also about a vacation. At the time that you were returning to San Francisco, you were involved in that accident; were you still on your vacation?

A. No, I don't believe I was.

The Court: Q. Well, you were on your own business? You were your own boss? You decided where the vacation began and ended, didn't you?

A. Well, no sir.

Mr. Gray: Q. What is your answer, were you on vacation or not? A. No, I wasn't.

Q. You weren't. Now you testified that you also came down to discuss with someone in San Jose the hauling of a load, is that true?

A. Yes, sir.

Q. Was that one of your purposes in coming down to San Francisco?

A. Well not my principal one, no.

Q. Was it one of your purposes?

A. One of my purposes. [59]

Q. It was one of your purposes to come to see about it. To whom were you going to go, to John Dowdell? A. Bob Dowdell.

(Testimony of Allan J. Warner.)

Q. Who is he?

A. He is listed in the San Jose directory as John Dodwell, Draymen. They have been there for years and years.

Q. And had you hauled for him before?

A. Yes I had.

Q. So that one of your purposes was to talk to him about hauling merchandise?

A. That's right.

Q. With this trailer and tractor, is that right?

A. Yes sir.

Q. Now when you returned to Willow Creek, was the trailer in the same condition? Had any more merchandise been taken out of it?

A. It was completely unloaded, with the exception of this range and some odds and ends of furniture to come back to San Francisco.

Q. Then if I understand you correctly, while you were making your return trip, someone had taken out the rest of the merchandise, except this range and this other item you mentioned?

A. Yes sir.

Q. So some of it was removed while you were en route back, is that right?

A. That's right.

The Court: Q. As I understand it, then, the only reason why you left there was as an accommodation to your sister, is that right?

A. Yes, it is.

Q. So that whatever was on the trailer would remain there until she found a place for them, or she made up her mind as to what you were to take

(Testimony of Allan J. Warner.)

back, is that true? A. Yes, sir.

Mr. Gray: Q. Now in wildeatting, as you describe it, is it customary or do you do that frequently—leave your trailer with merchandise to be unloaded while you do something else?

A. Yes, it is.

Q. Nothing unusual about it?

A. No, it is not unusual.

Q. You have done it before, have you?

A. Yes sir, I have.

Q. And in your experience in that business, is it customary, is it an ordinary or usual thing?

A. It is.

The Court: Well, you wouldn't ordinarily leave it behind to come back for it unless you knew—

A. Not on a trip that far.

Q. You wouldn't go that far unless you knew that you would have a load that would warrant your taking the trip back and forth? [61]

A. Yes sir.

Q. Because what you got for hauling that wouldn't pay you for coming down to San Francisco and going back again, then coming back to San Francisco? A. No, it wouldn't.

The Court: I see, all right.

Mr. Gray: Q. Well Mr. Warner, in telling the story about this incident, you have changed this story a number of times, haven't you?

A. No, I don't believe so, materially. The only thing is, something else happens to occur to me

(Testimony of Allan J. Warner.)

that somehow or other I have either overlooked or something.

Q. Well you told the story, didn't you, in the office of Mr. Bledsoe, Messrs. Bledsoe, Dana and Smith over here, these lawyers for the insurance company, haven't you? A. I have what?

Q. You told the story in the office of these lawyers for the insurance company, didn't you?

A. Just exactly how do you mean?

Q. Well I mean this:—

The Court: Well, they don't use the word "story". That would have a bad connotation. A child tells a story—it means something untrue. Use the word "version".

Mr. Gray: All right.

Q. You have given your version of the facts at the office [62] of the insurance company lawyers, didn't you? A. Yes sir.

Q. You did before this trial in the State Court?

A. Yes sir.

Q. You went over it with them, told them about it, is that right? A. That's right.

Q. And did you ever give them a written statement? A. Yes, I did.

Q. You did give them a written statement, too. And do you know whether or not you told them about hauling pipe and furniture for your sister?

A. I did not.

Q. You don't think you told them that?

A. I know I didn't.

Q. You didn't tell them that. And you testified

(Testimony of Allan J. Warner.)

to that before Judge Deasy, though, when we filed suit in the Superior Court, didn't you?

A. I believe I did.

Q. Well now—the testimony you gave before Judge Deasy, regarding the hauling of the pipe, and that which you have given today, that is true, is it?

A. Yes sir.

Q. That is the true version?

A. That is the true version of it. [63]

Q. And any other version you may have given is untrue?

A. No, I wouldn't say it was untrue. As I see it, the only thing that I have—I mean, that I can say—well, I have said it, I have no proof of it.

Q. I see.

The Court: Q. What you mean to say is that sometimes you omitted something. Why did you omit the facts that you were carrying—

I am going to ask this leading question, although you are cross-examining him too; but I am permitted to ask that to see what the answer would be, and to give him a chance to explain. I will put it that way.

Q. Did you leave that out deliberately, or did you just forget it or what?

A. No sir, the way I seen it, the way I understood, I was insured. It didn't seem to matter whether I had 10 ton or no tonnage or anything. The papers, the insurance papers as I read them, had nothing on them as far as I could understand

(Testimony of Allan J. Warner.)

about being without a trailer or with a trailer or anything with a load or without a load.

Q. Yes, but as to the trailer, the insurance said that it was for while you were carrying goods. Do you remember that portion of it?

A. No, I don't.

Q. You don't remember that? [64]

A. No sir, I don't.

Q. Well, now, why did you leave out that that was the purpose of the trip? The trip had that purpose; why did you leave it out?

A. Well—

Q. Why did you leave it out when you were testifying?

A. Well the way I seen it, it didn't seem important to me.

Q. It didn't seem important to you?

A. No sir.

Q. Well didn't it occur to you that that was an incident that you ought to tell about, as you would tell them about going on vacation?

A. No sir.

Q. It didn't occur to you? A. No sir.

The Court: I see. All right.

Mr. Gray: No further questions at all.

The Court: All right. Any redirect?

Mr. Cathcart: Yes, one or two questions, if your Honor please.

(Testimony of Allan J. Warner.)

Redirect Examination

By Mr. Cathcart:

Q. To whom did you report this accident, if you remember?

Mr. Gray: You mean at the insurance company?

Mr. Cathcart: Yes. [65]

A. I think it was—the first place I went, I believe, was this place I figured was 111 Pine, unless I am mistaken. I could be. I seen, I was sent from there to some place else. I believe it was an adjuster. What his name is, right now I don't remember. He came out and looked at the tractor, took my statement, and that's all.

Q. And did you pay him the premium that you were telling us about?

A. No sir, I didn't. I paid the premium at the offices of the Commercial Standard.

Q. Is that in San Francisco?

A. I believe it is.

Q. Now would that be the office of Commercial Standard or one of your, your own insurance agent?

A. No, I believe it was the agent or representative for the Commercial Standard.

Q. I see. And had you done business with him before?

A. No, not that I can ever recall.

Q. Well this policy, where did you get it?

A. Oh, I don't know just exactly how I got the policy, through somebody that knew somebody, and they referred me to the Commercial Standard or

(Testimony of Allan J. Warner.)

something like that. I don't know just exactly how it did come about.

Q. Well do you remember who actually delivered the policy to you? [66]

A. No, I don't.

Q. Nor where?

A. No, I don't know that either. It seems to me though, that it came in the mail.

Q. And you had talked, of course, to somebody about it beforehand, had you?

A. About the policy?

Q. Yes.

Mr. Gray: Objected to as incompetent, irrelevant, and immaterial. I don't see the need for this inquiry, especially on redirect.

The Court: I will sustain the objection. We are not talking about the circumstances of when the policy was entered into.

Mr. Cathcart: Surely.

Q. And there is of course a service by mail from this little town of Willow Creek to San Francisco, is there? A. What?

Q. Are there mail connections from Willow Creek to San Francisco?

A. Yes, I believe there are—rural.

Q. I see. As you went up to Eureka, were you aware that your premium was falling due?

A. That was the purpose of my making the trip.

Q. I mean as you went north?

A. As I went north. That was the purpose of

(Testimony of Allan J. Warner.)

my trip north, the [67] money from that to pay the premium.

Q. Oh, you mean—let me get this correct now. The money which you hoped to get from your sister for carrying this load north, you intended to use that in paying your premium, is that correct? A. To pay my premium, that's correct.

Q. I see. Have you ever discussed any of these matters with Mr. Gray, this gentleman here? (Indicating.)

A. No, not as far as I know.

Q. As far as you know, you had never seen him before the State Court action, is that right?

A. No, I hadn't. I don't believe so.

Q. Yes. He asked you about me, so I thought I would ask you about him.

The Court: All right.

Mr. Gray: Let's get this clear.

Recross Examination

By Mr. Gray:

Q. You saw me in the State Court and you saw me here, outside of that you never saw me?

A. No sir.

The Court: That is what he meant.

Mr. Gray: Q. Paying this premium, you paid it at the same place you customarily paid the premiums, always?

A. No, I didn't, I don't think. As a general rule I think it [68] was paid to the bank, and just exactly how it was done, I don't know; but it seems to me it was paid to the bank and then the bank

(Testimony of Allan J. Warner.)

paid it to the insurance company or something like that. Anyway, I went to this particular place where I was to pay the payment. First of all I went and notified the insurance company of the accident. I told them that I had a payment due, and they told me to hustle right down and make the payment. They told me to pay the premium, which I did. I had never been there before. It is the first time that I had ever been there. I believe it was on Pine Street, though.

Mr. Gray: That is all.

The Court: All right.

Mr. Cathcart: Just one or two questions.

Further Redirect Examination

By Mr. Cathcart:

Q. What was the name of your partner in this operation? A. Robert W. Woodrow.

Q. And are you and he still partners?

A. No sir, we are not.

Q. He is here in San Francisco?

A. I believe he is now.

Mr. Cathcart: Yes, that is all. Thank you.

The Court: All right, step down.

(Witness excused.) [69]

* * * *

Mr. Cathcart: All right, your Honor. Shall we discuss the instructions now?

The Court: No, if you are going to make a motion for a directed verdict, I will rule on that and then I will tell you about the instructions.

Mr. Cathcart: Yes. Well at this time then, if

your Honor please, I will make a motion for a directed verdict on the ground that it has been shown by evidence that at the time this accident happened, the vehicle, the Dodge tractor, was not being used for the transportation of merchandise within the meaning of the policy which is in evidence. [73]

Now the policy is very specific in its terms, and it is very clear. It says, "The automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows . . . and this insurance covers no other use or operation."

Now the law is very clear on the point that coverage will not be extended beyond the express terms of the policy merely because it would be nice to have the plaintiffs recover a judgment from the insurance company. A very slight departure from the uses for which the insurance exists has served on numerous occasions to rule out the liability on the part of the insurance company.

* * * *

[74]

Mr. Gray: Continued until tomorrow morning? The whole thing is continued until tomorrow morning?

The Court: Yes, I will continue the whole matter and re-open the case to allow you to re-amplify. Then we will excuse the jury and hear additional argument on the motion.

* * * *

[113]

Mr. Gray: Call Mr. Warner for further cross-examination. [115]

ALLAN J. WARNER,

recalled as a witness on behalf of the defendant,
previously sworn, testified further as follows:

Cross-Examination

By Mr. Gray:

Q. Mr. Warner, I had a discussion with you after the hearing yesterday, outside the courtroom, is that true? A. Yes, sir.

Q. Now in that discussion we discussed some of the facts pertaining to this case. Now yesterday you testified that one of your purposes for making this trip was to talk to John Dowdell, who is in the drayage business in San Jose, is that correct?

A. Yes, sir.

Q. And at the time of this accident, you were on U. S. Route 101, is that right?

A. That's right.

Q. And that is the most direct route, is it not, from the point where you left your trailer to San Francisco, and also to San Jose?

A. Yes, sir, it is.

Q. In other words, San Jose is below San Francisco, south of San Francisco?

A. That is correct.

Q. Now you also told us that you were in the wilcatting [116] business. I wish you would tell us a little more about that. That means, does it not, that you frequently take your equipment and go from place to place and haul for whomever will hire you? A. That's correct.

Q. Is that right? A. That's right.

(Testimony of Allan J. Warner.)

Q. In other words, you don't start always from your home at 10 Ord Street, San Francisco, you may start from any place where you happen to be, where you could locate a job, is that right?

A. That's right.

Q. Now is it true that in wildecating, it is common practice to sometimes take a trailer that is already loaded instead of your own trailer?

A. That is true, too.

Q. In other words you take your tractor and attach it to a trailer for some company or individual who has a load and then you attach your tractor to the trailer and drive the load for him?

A. That's right.

Q. That is common practice in wildecating, is it?

A. Yes, it is.

Q. And you were engaged in the business of wildecating, is that right? [117]

A. That's right.

Q. Referring now to Dowdell, do you know whether or not he has such trailers?

A. Yes, he does.

Q. He has such trailers. Now I believe you made the statement yesterday in Court that while you intended to see or communicate with Dowdell, you didn't do so?

A. No, sir, I didn't.

Q. All right. It is true that this accident disabled your tractor, is it not?

A. That's correct.

Q. The accident here involved. You had some emergency repairs made to the tractor at Scotia?

(Testimony of Allan J. Warner.)

A. I did.

Q. They tied it up for about a day, is that right? A. That's right.

Q. And then those were only emergency repairs, is that right? A. That's right.

Q. Then when you went from Scotia to San Francisco, did you take your tractor and have repairs made to it of a permanent nature?

A. In San Francisco.

Q. And in San Francisco your tractor was then tied up for some period of time because of repairs?

A. It was tied up for a day and a half. [118]

Q. A day and a half because of repairs. Now is that the reason why you did not communicate with Dowdell, because you didn't have your tractor available?

A. Well, I guess that would be as good a reason as any.

Q. Well the point is, you didn't have any tractor to haul, did you. A. No, sir.

Q. Well, let's get this clear. Did you own any other tractor? A. No, I didn't.

Q. Did you have any other equipment for hauling, other than this tractor and the trailer that was up at Willow Creek at that time?

A. Nothing licensed.

Q. At that time? A. Nothing licensed.

Q. Nothing licensed at that time?

A. That's right.

Q. All right.

The Court: Q. In other words, you couldn't

(Testimony of Allan J. Warner.)

and just tack it on and make a trip for someone? You said you had nothing licensed. By that you mean that you couldn't pick up another trailer and hitch it on to your tractor?

A. Not my own trailer.

Q. You would have to have a licensed trailer?

A. A licensed trailer. [119]

The Court: I see. All right.

Mr. Gray: Q. Well these trailers you say others had, like Dowdell, those were licensed trailers?

A. Yes, they were.

Q. But you had no other licensed trailer other than the one you left at Willow Creek?

A. That's right.

Q. Well then, as far as the tractor itself, in your wildecutting, have you ever used that for hauling merchandise?

A. Yes, sir, I did.

Q. And what have you hauled in that?

A. I have hauled practically every commodity.

Q. And I believe you told me you hauled burlap sacks, about 700 pounds of burlap sacks with that?

A. Yes, I did.

Q. So you can use that equipment for hauling?

A. Yes, you can.

Q. And you did use it for hauling?

A. I have used it many times.

Q. And under this same permit that you had, you used that tractor for hauling?

A. Yes, sir.

Q. I think I asked you this question: In your wildecutting work, much of your work is for other

(Testimony of Allan J. Warner.)

haulers? A. Yes, it is. [120]

Q. In other words, they are subsidizing you—they have something to haul and for some reason or other they don't have enough equipment available, then they let you do the hauling for them and they pay a certain percentage or some amount for it, is that right? A. That's right.

Q. And that is why you frequently take their trailer instead of your own, if they have it loaded, is that correct? A. Yes, sir.

Q. And attach it to your tractor. Then you told me, didn't you, that you went back to get your trailer after the repairs had been made, because you had been in communication with Augustine V. Fries? A. That's right.

Q. He was a regular customer of yours?

A. He was a produce merchant.

Q. I mean he was a man you had worked for before? A. Yes, sir.

Q. And you went to get the trailer in order to have it available for him, is that correct?

A. That's right.

Q. Working for him.

A. (Witness nodded in the affirmative.)

Q. And for hauling? A. For hauling.

Q. Yes. Now I notice, Mr. Warner—

Mr. Gray: Counsel, I will call your attention to the testimony before Judge Deasy in the Superior Court on Page 7, line 17, over to page 8—say about line 3.

Mr. Cathcart: All right.

(Testimony of Allan J. Warner.)

Mr. Gray: Q. I will call your attention in your testimony before Judge Deasy, where, instead of referring to "Willow Creek," you refer to "Blue Lake". Do you recall that or would you like to look at the testimony?

A. Well as far as I know, it is one and the same.

Q. Well look it over. I don't want to confuse you. That was under cross-examination before Judge Deasy.

(Handing to witness.) I have marked it in the margin there, Mr. Warner. When you have read that, turn the page. I think I have got three lines on the other page. Have you read it?

A. Yes, I have.

Q. Thank you. This reads as follows: (Reading.)

"Q. Now calling your attention to the date of the accident, June 22, 1946, you were driving this Dodge Truck, is that correct? "A. Yes, sir.

"Q. What direction were you going?

"A. I was heading South.

"Q. And where had you been? [122]

"A. I had been to Blue Lake.

"Q. And that is in Lake County, is it?

"A. That is in Lake County.

"Q. Well had you left what you call the device in the back, the trailer? "A. The trailer.

"Q. Had you transported the trailer up there?

"A. I had taken the trailer up with a load of pipe.

"Q. Where had you taken it?

(Testimony of Allan J. Warner.)

“A. To Blue Lake.

“Q. From where?

“A. From San Francisco.”

Now these questions were asked of you and those answers were given by you before Judge Deasy, were they? A. That's right.

Mr. Gray: I might state, counsel, that as to Lake County, I think that was a mistake that was corrected later. It was my fault. I said “Lake County” because I happened to know there was a Blue Lake in Lake County, so I am not holding the witness to that point. The question was wrong.

Mr. Gray: Q. The point I am making is, is it Blue Lake or Willow Creek?

A. Well, it is Blue Lake, if I remember correctly.

Mr. Gray: Is it on there? [123]

Mr. Cathcart: Willow Creek and Blue Lake. (Indicating)

Mr. Gray: Well here, counsel showed me a map. His eyes are a little better than mine. (Examining map.) He has taken a pencil and circled a place called Blue Lake. He has also taken a pencil and circled a place called Willow Creek, also Eureka is circled.

Q. Now would you look at that map—can you see this? If you will hold it? Look at the map and see whether that will help you straighten us out. (Handing to witness.)

A. It is all on a direct route.

(Testimony of Allan J. Warner.)

Q. Well I realize that. In other words, you probably drove through one or the other?

A. You go through all three.

Q. Where did you go, where did you dump the load of pipe and furniture, or whatever it was?

A. At Willow Creek.

Q. Willow Creek?

A. You get to Willow Creek, and you have to go through Blue Lake, I believe.

Q. Oh, Blue Lake. According to that map, that seems to be quite a distance.

A. I don't know what the scale is.

Mr. Gray: I don't know if a scale is on here. Is there a scale on here, counsel, do you know?

Mr. Cathcart: Yes, I believe there is. [124]

Mr. Gray: Oh, yes.

Q. Well according to this scale, it was at least 20 miles or more?

A. That's right.

Q. Well, so then, when you testify in one proceeding about Willow Creek and in another about Blue Lake, you have reference to one and the same place?

A. That's right.

Q. Well which place do you have reference to?

A. Willow Creek.

Q. You have reference to Willow Creek? and not Blue Lake?

A. Yes.

Mr. Gray: Thank you, counsel. (Handing map to Mr. Cathcart.)

No further questions.

(Testimony of Allan J. Warner.)

Redirect Examination

Mr. Cathcart:

Q. Now on this trip to San Francisco when you were in the tractor and when the accident happened, you tell us this morning, after having talked with Mr. Gray, that you had the intention of seeing Mr. Dowdell in San Jose, is that correct?

A. That's correct.

Q. Did you see him? A. No, I didn't.

Q. Had you been in communication with him before you went to San Jose? A. Yes, I had.

Q. You had? When?

A. The month prior to that.

Q. When you were down in San Francisco, is that right? A. That's correct.

Q. And had you hauled for him during the month prior to that? A. I had.

Q. And during that month, whose trailer had you used? A. My own.

Q. Your own? A. Yes.

Q. And when did you next see Mr. Dowdell or speak with him or have any communication with him after this accident? A. In July.

Q. In July of the following year?

A. Of the following month.

Q. I mean, the following month, yes.

A. Yes.

Q. I see. At about what time in July, do you recall?

(Testimony of Allan J. Warner.)

A. Somewhere between the 8th, I should say, and the 26th.

Q. I see. Then you testified yesterday that you were not transporting any merchandise at the time of the accident, is that correct? [126]

A. That's correct.

Q. And accordingly, although you testified this morning for the first time that you occasionally carried loads on your tractor, you were not carrying any load on your tractor at the time of this accident, is that correct? A. That is true.

Q. On what occasions had you carried loads on your tractor?

A. I have carried loans on the tractor many times.

Q. Well, tell us some of those occasions.

A. Oh, I think it was the Sunday—let's see, I don't know what day that would have fallen on. I think it was the Sunday, about the 28th, from the 20th of June through August—July, August, and September, I hauled sacks down into the valley on the tractor. I hauled 10,000 sacks.

The Court: Q. How much of a load could you carry?

A. About 700 pounds.

Q. That is all? A. That is all.

Q. In other words, you couldn't carry sack material, like cement or sand or anything else?

A. Oh yes, I could.

Q. Well what did you actually carry, empty sacks? A. Empty sacks in bales.

(Testimony of Allan J. Warner.)

Q. That you tie? A. Tie, yes. [127]

Q. Had you ever carried loads for this Mr. Dowdell like that? A. No, I never did.

Q. What kind of hauling did he do?

A. General merchandise, general freight, everything.

Q. And the particular work that you had in mind wouldn't be that type, or would it be—what?

A. No—for the tractor alone?

Q. Yes. A. No, it wouldn't.

Q. It wouldn't be? A. No.

The Court: I see, all right.

Mr. Cathcart: Q. Now, you testified that you were hauling sacks on the 28th of June; of what year would that be? A. That was '46.

Q. Well now how long after the accident was that? A. I should say about five days.

Q. Five days after the accident. And where was that hauled? A. That was to Hayward.

Q. From where? A. San Francisco.

Q. Then during the period from five days after the accident, for the rest of June and all of July, August, and September, you were hauling sacks on your tractor, is that correct? A. Yes, sir.

Q. Where was your trailer all that time?

A. In San Francisco.

Q. And on this particular job, you did not use your trailer, is that correct?

A. I didn't, that's right.

Q. Who was this man Fries that you refer to?

A. He is a produce broker.

(Testimony of Allan J. Warner.)

Q. Is he the man for whom you hauled the sacks? A. That's right.

Q. Where is his office?

A. He had a place on California street.

Q. Here in San Francisco? A. Yes.

Q. Yes. Now Mr. Gray referred to a point of your testimony which you gave when you were being examined by him in the state court. You went down as far as page 8, line 3; now I will ask you to read from there on to page 10, line 19, and ask you if those questions were asked you by Mr. Gray and if you gave those answers.

Mr. Gray: What is this, cross-examination?

Mr. Cathcart: No, this is putting it all in, putting in the entire testimony.

Mr. Gray: I have no objection. Put the whole thing in if you want.

The Court: I will say, gentlemen, the position of this [129] witness has changed. It is quite evident at the present time that he is being used to establish some affirmative facts which were not brought out on direct examination, which may be contrary to what was brought out; so to that extent he has become your witness, and we cannot stand on the technicality that he is not your witness.

Mr. Gray: Well, I have no objection to him reading this into the record, your Honor.

The Court: I see. All right. I just wanted the record straight, that is all.

Mr. Gray: What line is that?

Mr. Cathcart: Excuse me.

(Off the record discussion between counsel.)

(Testimony of Allan J. Warner.)

Mr. Cathcart: Q. Now were those questions asked you by Mr. Gray in a proceeding in the State Court? And did you give those answers?

A. I did. I guess I did.

Mr. Cathcart: Well, I take it, counsel, it is stipulated that you did ask him those questions and that he did give those answers?

Mr. Gray: I have no objection to you reading any part of this to the jury.

Mr. Cathcart: Then, ladies and gentlemen of the jury, I will continue on from where the witness read when he was being asked by Mr. Gray to read his testimony in the state court. [130] You will recall that he said—this is on page 8, line 1, of his testimony in the state court: (Reading.)

“A. I had taken the trailer up with a load of pipe.

“Q. Where had you taken it?

“A. To Blue Lake.”

And as the map shows, Blue Lake is a little town between Eureka and this little community of Willow Creek. It is a little—just a moment, I might get the map so that we can see it.

“Q. From where?

“A. From San Francisco.

“Q. From some company?

“A. Not for some company, for a relative that had a summer home up there.

“Q. You transported pipe for a relative?

“A. That’s right.

“Q. Were you ever paid for it?

(Testimony of Allan J. Warner.)

"A. Yes, I got \$75 for the haul.

"Q. And you brought the pipe to Lake County?

"A. That's right."

Again, Lake County means this little community, Blue Lake or Willow Creek, whichever it is.

"Q. And you brought the pipe to Lake County?

"A. That's right.

"Q. And you left the trailer there, did you?

"A. That's right. [131]

"Q. With the pipe on it?

"A. No, the pipe had been taken off.

"Q. Well what was your destination at the time of this accident?

"A. I was on my way back to San Francisco.

"Q. Well, did you intend to come back to get the trailer? "A. I did.

"Q. And you eventually did go back to get the trailer? "A. I did.

"Q. When did you do that?

"A. About five days later.

"Q. Was anybody traveling with you?

"A. No, the second trip, no."

That is the second trip, when he drove back to get the trailer.

"Q. At the time of this accident?

"A. At the time of the accident, my wife was with me.

"Q. What is her name?

"A. Mrs. Jane Warner."

There is a question mark over "Jane."

Mr. Cathcart: Q. Is your wife's name Jane?

(Testimony of Allan J. Warner.)

A. It is June.

“Q. Is she in Court? “A. No, sir.

“Q. Where does she live? [132]

“A. Number 10 Ord Court.”

Q. Now those questions were asked by Mr. Gray and those answers were given by you in the State Court? A. Yes.

Mr. Gray: Continuing, it goes on: (Reading.)

“Q. Well, had your wife been with you from the time you started out from San Francisco with the pipe? Did you take her along with you?

“A. No, she had been up there on vacation.

“Q. She was in Lake County?”

In Blue Lake, I take it.

“A. That’s right.

“Q. Let’s see if we have the facts right. Your wife was at Blue Lake, Lake County, and you were in San Francisco? “A. That’s right.

“Q. And a relative of yours ordered a load of pipe and you agreed to transport the pipe to Lake County for this relative for a certain sum of money, is that right? “A. That’s right.

“Q. And were you paid that money?

“A. That’s right.

“Q. And that went into the partnership, is that right? “A. That’s right.

“Q. Then you took the trailer and the tractor that were hitched together with a load of pipe and went from San Francisco [133] to Lake County?”

Again, Blue Lake.

“A. Yes, sir.

(Testimony of Allan J. Warner.)

“Q. And there you disconnected the tractor and left the pipe, you disconnected the trailer from the tractor and left the pipe in Lake County? Is that right?”

Well, Blue Lake again, I guess.

“A. That’s right.

“Q. At the time of this accident, you were returning to San Francisco? “A. That’s right.

“Q. You were returning back to continue with your business?

“A. No, I had a definite purpose in coming down, I might state. I had a payment due on my insurance policy Monday. My policy would lapse if I did not get in here Monday. That was the reason for coming down Frisco, here.

“Q. So you came down for that business?

“A. That’s right.

“Q. And when did you intend to return for your tractor? “A. The following day.

“Q. For your trailer?

“A. The following day.”

I take it that Mr. Gray said “tractor” when he meant “trailer”, so he corrected the question. [134]

“A. The following day.”

Mr. Gray: I may say, counsel, that during that trial I thought it was a truck, and sometimes I called it a truck and sometimes a tractor. I meant the same thing.

Mr. Cathcart: Yes. (Reading.)

“Q. That would have been Tuesday?

“A. Yes.

(Testimony of Allan J. Warner.)

“Q. And what day did this accident occur?

“A. That happened on a Saturday.

“Q. Now going back to the Dodge Tractor, that was registered with the Department of Motor Vehicles, wasn't it? “A. With the what?

“Q. It was registered with the Department of Motor Vehicles like an automobile? “A. Yes.

“Q. That was registered in your name and Mr. Woodrow's? “A. That's right.

“Q. As joint owners, and you were using it that day and Mr. Woodrow knew you were using it?

“A. That's right.”

That is all I care to read from this at this time.

Mr. Gray: Do you want to read the rest of that down there? It is on the subject. Why don't you finish the subject?

Mr. Cathcart: If it is pertinent, I don't want to exclude [135] anything.

Mr. Gray: It has a bearing on the subject. You might as well read it. Go right on where you stopped.

Mr. Cathcart: All right. Page 10, line 15. (Reading.)

“Q. As joint owners, and you were using it?

“A. That's right.

“Q. And the money you got from that job went into the partnership? “A. That's right.

“Q. Now, do you recall driving south of Scotia toward this bridge? “A. I do, yes.

“Q. Do you remember this quite well?

“A. I do.

(Testimony of Allan J. Warner.)

“Q. By the way, you stopped at Scotia and serviced your truck? “A. That’s right.

“Q. You put air in the tires, is that right?”

I don’t believe that this deals with the subject that I intended to bring out.

Mr. Gray: O.K.

Mr. Cathcart: Q. Now, Mr. Warner, I call your attention to a copy of the transcript of your testimony before Judge Goodman and I believe you read part of this, you read page 6, lines 3 to 12. Mr. Gray asked you if you had given answers [136] to his questions, and then he read that testimony to the jury. Now would you read the rest of that page, down through page 7, line 1? (Handing to the witness.)

Mr. Gray: Where did he start, counsel?

Mr. Cathcart: Where you left off.

Mr. Gray: Now I was on page 6.

Mr. Cathcart: I asked him to read from there down to page 7, line 1.

(The witness examined a copy of the transcript referred to above.)

Mr. Gray: Counsel, I think Mr. Warner has finished.

Mr. Cathcart: Have you finished it? I am sorry, Mr. Warner.

Q. And do you recall if those questions were asked you by Mr. Bledsoe when you were before Judge Goodman in this matter and did you give those answers? A. I believe I did.

Mr. Cathcart: Yes. And then I will just, so

(Testimony of Allan J. Warner.)

that we can get a little better continuity, repeat the part that Mr. Gray read. This was a question by Mr. Bledsoe to this gentleman when he was testifying before Judge Goodman in this part here. In fact, it was in this room: (Reading.)

“Q. This trip was in the nature of a vacation trip for you, wasn’t it?

“A. It was a combination. [137]

“Q. What was the nature of the combination?

“A. Business had been very slow about that time of the year and we had gone up into Willow Creek for an outfit up there, California Barrel. We had intended, if possible, to haul barrels out of Willow Creek.

“Q. Did you see someone while you were up there about that? “A. No, I didn’t.

“Q. How long did you stay up there?”

This is the part that was read yesterday, that I just wanted to read so that you could get the entire picture of the thing. (Continuing.)

“Q. How long did you stay up there?

“A. I was up there about two weeks, I believe.

“Q. And was this during your vacation time?

“A. Yes, sir.

“Q. Then on the way back, did you do anything but just drive home?

“A. No, not at all.

“Q. And the purpose was simply to get home?

“A. That’s right.

“Q. You were not transporting any commercial goods at that time? “A. No, I wasn’t.”

(Testimony of Allan J. Warner.)

The Court: Was he speaking of the final return home? [138]

Mr. Cathcart: Well, he is being asked about the accident trip.

The Court: Oh, the accident trip. All right.

Mr. Cathcart: Yes, sir.

The Court: I just wanted to make sure. All right.

Mr. Cathcart: Q. And I will also ask you to read page 5, line 7, down to page 6, line 2, just to get the whole story here. (Handing to witness.)

Mr. Gray: Counsel, while the witness is reading that, will you stipulate that this transcript that you are now showing him was a default proceeding conducted by Mr. Bledsoe, of your office, in which I was not present, nor did I participate. Will you so stipulate?

Mr. Cathcart: Surely.

Mr. Gray: Thank you.

Mr. Cathcart: I assume that what you have stipulated was a fair proceeding, conducted before Judge Goodman who was known for fairness?

Mr. Gray: I will stipulate to the fairness of Judge Goodman any day, today included.

The Court: All right, now that all the amenities have been provided for, taken care of, let's go on, gentlemen.

Mr. Cathcart: Now the additional material that I wanted to read was simply this: (Reading.) [139]

“Q. That accident occurred on Highway 101 in

(Testimony of Allan J. Warner.)

the County of Humboldt, three miles south of the city of Scotia, is that right?

"A. That's right.

"Q. At the time of the accident were you driving a 1939 Dodge Truck, number 8702218, is that right? "A. That's right.

"Q. And that tractor had no trailer or anything behind it at that time? "A. Also right.

"Q. And accompanying you on your trip was your wife and some child or children?

"A. No, I was with my wife only.

"Q. The trip had been taken to what town?

"A. Willow, Willow Creek.

"Q. You were taking your mother-in-law or mother up there? "A. My mother.

"Q. Was your wife along?

"A. Yes, on the way home.

"Q. Oh, on your way home, your wife was coming back with you? "A. That's right." [140]

Mr. Cathcart: Well, perhaps counsel is willing to stipulate to this. That same exhibit, if your Honor please, to the answer, we have set forth a copy of a reservation of rights agreement under which this gentleman was defended by our firm in the State Court, and I take it counsel has no objection to stipulating it was executed?

Mr. Gray: I will stipulate to its authenticity, your Honor; if counsel states it was signed, it is good enough for me. But I do not stipulate to its admissability. [141]

* * * *

(Testimony of Allan J. Warner.)

The Court: Yes; well, if counsel will not accept the stipulation, I think I will overrule the objection and have it introduced as an exhibit so that the jury may, if they desire, examine it, and satisfy themselves of the terms. [142]

* * * *

The Clerk: Defendant's exhibit A in evidence.

DEFENDANT'S EXHIBIT A

Leighton M. Bledsoe, Law Offices of Cooley, Crowley, Gaither & Dana, 206 Sansome Street, San Francisco 4; DOuglas 7828.

San Francisco, California
August 26, 1946

Commercial Standard Insurance Co.
Fort Worth, Texas
c/o Cooley, Crowley, Gaither & Dana
206 Sansome Street
San Francisco, California

Re: George W. Boulter and Margretta Boulter v. Allan J. Warner, Robert W. Woodrow, et al.—San Francisco Superior Court No. 356235, Comm. Stand. Ins. Pol. No. MC 170330.

Gentlemen:

This is to advise you that we, and each of us, agree that you, and any of your representatives and attorneys, may participate in any investigation and/or defense of the above mentioned claim by George W. Boulter and Margretta Boulter, and of

(Testimony of Allan J. Warner.)

that certain action numbered 356235 in the Superior Court of the State of California in and for the City and County of San Francisco brought by said Boulters against us; and that any such action taken or to be taken by you, or any of your representatives, is entirely without prejudice to any rights and defenses of the Commercial Standard Insurance Company under the above described, and any, insurance contract; and any such participation does not and shall not constitute an admission of liability on the part of said Commercial Standard Insurance Company.

It is likewise understood by us, and each of us, that nothing herein contained shall prejudice the right of either the Commercial Standard Insurance Company or of the undersigned to apply to any court of competent jurisdiction at any time for a determination of the rights of the parties with respect to said or any, contract of insurance.

We do, and each of us hereby does, waive any right that we, or either of us, may have to claim that the Commercial Standard Insurance Company waives, has waived, or shall waive any right to deny liability under said, and any, contract of insurance. At the same time, we in no way waive any of our rights against the Commercial Standard Insurance Company under said contract.

Very truly your,

/s/ ALLEN J. WARNER,

/s/ ROBERT W. WOODROW.

The Court: All right.

(Testimony of Allan J. Warner.)

* * * *

Mr. Cathcart: Q. You told us yesterday that at that time you made your statement to the insurance company about what happened, and at that time, you didn't mention any of this carrying pipe and furniture and that sort of thing—it just hadn't occurred to you, or you didn't think it was pertinent, is that correct? [143]

A. That's correct.

Q. And in your discussion with Mr. Gray yesterday afternoon, just what was the tenor of that discussion yesterday afternoon, do you remember? Did he suggest that perhaps there were some things that you hadn't thought of or just how did that come up?

A. No, I don't know just exactly how it came out.

Q. Do you remember how long he and you talked? A. About ten minutes, I imagine.

Q. About ten minutes. And you talked about the things you talked about this morning on the stand, is that correct?

A. Whatever has been discussed here.

Q. I see. Do you recall when you were paid the \$75 by your sister for carrying this pipe up there?

A. Do you mean the day before or the day after, or when I was paid?

The Court: Well, when, if at all, before you returned to San Francisco and after you got there.

The Witness: I was paid the night before I left.

(Testimony of Allan J. Warner.)

The Court: All right, the night before you left. All right.

Mr. Cathcart: Q. You were paid the night you left? A. That's right.

Q. And how much did you receive?

A. \$75. [144]

Q. In what form of money?

A. Traveller's check.

Q. A traveller's check? A. That's right.

Q. What kind of a traveller's check? If you remember.

A. I don't know, just a traveller's check.

Q. I see. And it was endorsed by whom?

A. By my sister.

Q. And did you cash it? A. Yes, I did.

Q. Where?

A. At a service station I do business with.

Q. In San Francisco? A. Yes, sir.

Q. I see. And you paid that, I believe you said, as a premium on your insurance? A. I did.

Q. When?

A. On the following Monday, I believe.

Q. On the following Monday? A. Yes.

Q. That is the Monday following this accident?

A. That's right.

Q. Then what day was the accident?

A. Saturday. [145]

Q. And I believe you said you went back to Scotia to have some temporary repairs done on your tractor, is that right? A. That's right.

Q. And when did you leave Scotia?

(Testimony of Allan J. Warner.)

A. The evening of the accident.

Q. That would be Saturday evening?

A. Saturday, afternoon, late.

Q. And then you got to San Francisco early Sunday morning?

A. No, sir, I got to San Francisco—it was about 11 o'clock.

Q. Eleven o'clock at night? A. Yes.

Q. And—

The Court: Please don't repeat the answer. We all fall into that habit. It is confusing; unless the reporter knows your habits, he will put it down as another answer, and it is confusing in the record.

Mr. Cathcart: Well I am sorry, your Honor.

Mr. Cathcart: Q. When did you see the insurance company then? A. Monday morning.

Q. Did you pay the premium at that time?

A. I did.

Q. How much was it, do you remember?

A. \$33.

Q. \$33? [146] A. That's right.

Q. Was that the regular premium or was that what it was always? Do you know how it happened to be \$33? A. No, I don't.

Q. Did you answer the question?

A. Yes, I did. I don't know.

Q. You don't know how it happened to be \$33?

A. No, I don't.

Q. You told us yesterday, that your purpose, I believe, in carrying this pipe was to get money for your insurance policy, is that correct?

(Testimony of Allan J. Warner.)

A. That's right.

Q. Were you at this Blue Lake area about a week before returning to San Francisco or about two weeks?

A. I don't know now. It was too long ago.

Q. When did you receive \$75, just after you got there?

A. No, the night before I left for San Francisco.

Q. Oh, I see, not until you were ready to leave?

A. That's right.

Q. Was that for all the work you did or just for the carriage of this freight?

A. That was for the carriage of the freight.

Q. What time of day, do you recall, were you paid off? A. About nine o'clock at night.

Q. Nine o'clock. And what night would that be?

A. I don't remember.

Q. I see. But at any rate, just before you left for San Francisco? A. That's right.

Q. I believe you testified you left for San Francisco about 5:00 o'clock in the morning.

A. That's right.

Q. Yes. Now just exactly where was this job of fixing the pipe done, was that in Willow Creek? Now we have talked about different places, so could you fix in your mind and tell us just where that was?

A. No, I don't think I can, to be truthful with you.

Q. Well, was it on a farm somewhere?

(Testimony of Allan J. Warner.)

A. It was in a little mining—well, it was on a piece of mining property.

Q. That is where your sister's home is?

A. That's right.

Q. I see. And is it near Willow Creek or near Eureka or near Blue Lake?

A. No, it is—I believe it is in Willow Creek, and as I understand it, it is on the south fork.

Q. I see. And what kind of a community is Willow Creek, is it a large community or a very small one? A. It is very small.

Q. And what about Blue Lake, is that a small community also? [148] A. It is.

Q. I suppose Eureka is a pretty good sized town? A. It is.

Q. Now this testimony that you gave a few minutes ago about having it in your mind to see Mr. Dowdell when you came down on this trip, did you have that in mind when you left on the first trip south?

Mr. Gray: I don't quite understand that—the first trip south, counsel?

Mr. Cathcart: Q. The trip on which the accident happened? A. I did.

Q. When did that first enter your mind?

A. Well, it was my intentions when I went up there; I had my work.

Q. That is when you left San Francisco?

A. That's right.

Q. You intended to return from Eureka to see Mr. Dowdell in San Jose? A. That's correct.

(Testimony of Allan J. Warner.)

Q. And when you left San Francisco, you had your trailer on and you intended, did you not, to go up to Eureka, to that area, and unload your trailer and then bring it back? A. I did.

Q. And you intended, after bringing your tractor and the trailer back to San Francisco, to go to San Jose and see if [149] Mr. Dowdell had some hauling you could do for him, is that right?

A. Yes.

Q. I suppose Mr. Dowdell is a man you have done a good deal of business with in the past?

A. I have.

Q. And you kind of always had that intention, of getting another job from Mr. Dowdell?

A. No, I worked for him regularly.

Q. You worked for him regularly?

A. I worked for him regularly?

Q. I see. So that you didn't really have to get in touch with him beforehand? A. Yes, I did.

Q. You would phone him up from San Francisco, would you? A. Not necessarily.

Q. Sometimes you would go right down and see him? A. That's right.

Q. But other times you would call him from San Francisco and ask him about a hauling job?

A. That's right.

Q. So that you always regularly worked for him, and your state of mind on this trip was really no different from what your state of mind was at any other time? A. Yes, it was. [150]

Q. It was—in what way?

(Testimony of Allan J. Warner.)

A. Well the fruit starts to move about that time of year.

Q. I see. And how long have you been in this trucking business?

A. I have been in it all my life.

Q. Well that happens every year, then, doesn't it, that the fruit starts to move about that time of year?

A. That's right.

Q. So that your state of mind wouldn't be any different from what it would be any year at that time of year?

A. Yes, it was.

Q. In what way?

A. That was a poor season for the fruit.

Q. Well, nevertheless, did Mr. Dowdell haul fruit?

A. Mr. Dowdell hauls fruit.

Q. But even though it was a poor season, you expected to go down and see if you could haul fruit?

A. Yes, and see him if possible.

Q. So that your intention was fundamentally one of hauling fruit for Mr. Dowdell at this time of year?

A. Or somebody else.

Q. Surely, and that was always your intention at that time of year?

A. Yes, that's right.

Q. So that there was nothing peculiar about this trip from [151] Eureka down to San Francisco which was tied up with your intention of seeing Mr. Dowdell about hauling fruit for him at that time of year?

A. That's right.

Mr. Cathcart: I think that is all, your Honor.

Mr. Gray: Just one question here.

(Testimony of Allan J. Warner.)

Re-Cross Examination

Mr. Gray: Q. Counsel questioned you about this premium of 33. Is that the monthly premium?

A. (Witness hesitated.)

Q. Well it wasn't the yearly premium, was it?

A. No, it wasn't; I believe it is a monthly premium. I am not positive, though.

Mr. Gray: Is that right, counsel?

Mr. Cathcart: It is on the policy.

Mr. Gray: Monthly premium, yes. All right.

Mr. Gray: That is all.

The Court: Just one question I would like to ask.

Q. Tell, me, why is it that on previous occasions—I think I asked you this yesterday and I will ask you again in view of the fact that you have amplified the story you told yesterday. Why is it that in some of these proceedings when you were before Judge Deasy and when you were before Judge Goodman, you never said anything about any contract, about hauling pipe, and being paid for it, but talked only about going on vacation? [152] Why is it that you admitted that fact?

A. Well there are just things that seem to me that— (Hesitating)

Q. Well my hearing is perfect; just look at the jury.

A. (Continuing) They seemed not important. After having time to think about them, and thinking about other things, well, I guess they did seem important.

(Testimony of Allan J. Warner.)

The Court: I see.

Mr. Gray: May I ask a question on that?

The Court: Yes.

Mr. Gray. Q. You had quite a number, or some conversations with insurance adjusters of this company on the subject, too, didn't you, before you went to Judge Deasy? A. I did.

Q. And do you remember whether you told them about the pipe or not? Did they tell you not to mention pipe?

A. No, they didn't, as far as I can remember.

Q. Do you know whether you told them about the pipe? A. I don't remember.

Q. Well, did you tell them all the facts as you then remembered them?

A. In the statement, sir, everything that I said—the questions were asked me, and to the best of my knowledge as they were asked, I would answer them. [153]

Q. All right, let me ask you this question, then: Did the insurance adjuster ask you whether you were carrying any cargo? A. No, he didn't.

Q. He didn't? A. Not as far I know.

Mr. Gray: I see. That is all.

The Court: Q. So far as you know, when was the first time that you mentioned to anybody, whether in court or out of court, the fact that you were not only on vacation, but were also carrying a load of pipe when you went up?

A. I couldn't answer that.

Q. You couldn't answer that. By the way, you

(Testimony of Allan J. Warner.)

said that you made a report of the accident. What do you mean, that you reported it to the insurance company or the official report that you are required to make under the Motor Vehicle Act whenever you have an accident involving property?

A. The California Highway Patrol was at the accident. He took all the notes of the accident.

Q. He took all the notes? A. Yes.

Q. And you signed those notes, or signed a statement?

A. There was no statements, no citations of any kind.

Q. Well that isn't the point. You are required, you know, under the law, that whenever you are in an accident which [154] involved damage to property, even if you run against a parked automobile, you are supposed to make a report?

A. That's right.

Q. You had to state to the Motor Vehicle Department all about it. Now of course if there is an officer there who takes your statement, you don't need to make a report. That is your report. Is that what you mean?

A. That is what I mean. I notified my insurance company.

Q. All right, when you talked to the officers, did you tell them about the trip at all, do you remember? How you happened to be going back?

A. No, sir, I don't believe I did.

Q. Well when you saw the insurance company after you came to San Francisco, did you tell them

(Testimony of Allan J. Warner.)

about the trip and the details that you have given us now? That is, that you went on vacation and that you also made it a combination trip?

A. I believe that is the way I gave it—as a combination trip—business and pleasure. I am not positive.

Q. You are not positive? A. No.

Mr. Gray: Well let me ask just this question:

Q. You did testify, of course, before Judge Deasy, about the pipe, you remember that?

A. I believe so.

Q. You told me that here today. [155]

A. Yes, yes.

Q. Now at the time you testified here before Judge Deasy, that was the file of the action which the Boulters were suing for damages and got a judgment which we have talked about, is that right? A. I believe it is.

Q. That is the file for that action, no question about that. And in that file I was representing the Boulters—you remember that? And Rogers Smith of Dana, Bledsoe, and Smith, of which Mr. Cathcart is a member, was representing you and your partner—what is his name?

A. Woodrow.

Q. Yes, Woodrow. You remember that you were examined by Mr. Smith on direct examination about the case, is that right?

A. That's right.

Q. Now in my cross-examination, you told me about the pipe and we read it here, is that right?

(Testimony of Allan J. Warner.)

A. That's right.

Q. Now up to the time—

Mr. Cathcart: Excuse me, you examined him under 2055, without having first been examined by Mr. Smith.

Mr. Gray: Well, Smith examined him later, but I examined him under cross-examination.

The Court: All right, the main point is whether it was brought out at that time, and how it was brought out is not [156] important.

Mr. Gray: Q. Now before you testified at that trial, did Mr. Smith, your attorney, go over the facts with you, or discuss them with you?

A. Yes, he did.

Q. He discussed the facts with you?

A. Yes.

Q. And when you discussed the facts with your attorney, Mr. Smith, did he ask you why you were going, and did you tell him about the pipe?

A. I don't remember.

Q. You don't remember. But you do know you discussed the facts? A. Yes.

Q. As far as you know now, did you tell him the truth—Mr. Smith? A. Yes, I did.

Q. You told the truth to him, you didn't hold anything back that you know of? A. No, sir.

Q. All right, now at the time that I cross-examined you in that case, when I was representing the Boulters in this damage action, had you ever seen me before? A. No, sir.

Q. In your life? [157] A. No.

(Testimony of Allan J. Warner.)

Q. Have you ever talked to me over the telephone? A. Not that I know of.

Q. Did you ever talk to anybody that purported to be a representative of me or the Boulters before that? A. No, I never did.

Q. So you were there defending yourself in that case, is that right? A. Yes, that's right.

Mr. Gray: That is all.

Further Redirect Examination

Mr. Cathcart:

Q. Now on your report to the insurance company, you gave that about June 24th, 1946, didn't you? That would be, I believe, two days after this accident? A. That's right.

Q. And you talked to some adjuster for the insurance company? A. That's right.

Q. And you told him all of the facts?

A. That's right.

Q. And did they write down more or less what you told them?

A. Yes, they asked me questions, or he asked me questions, and to the best of my knowledge, I would answer them.

Q. Surely. And did he prepare a statement?

A. He did. [158]

Q. For you to sign? A. Yes, he did.

Q. And you, of course, read the statement over and signed it, is that right? A. I did.

Q. And I ask you if this is that statement. This is an exhibit in the proceedings before Judge Good-

(Testimony of Allan J. Warner.)

man. Look it over at your leisure and tell us if that is your statement. (Handing to witness.)

A. Well—(Hesitating)

The Court: Well, you don't need to read it word for word, just look it over. You are reading it word for word. Just see whether you signed it.

Mr. Cathcart: Q. And is that your signature on that statement? A. It is.

Q. And you signed at the bottom of each page, did you not? A. I did.

Q. And you read the statement over before signing it, is that correct? A. I did.

Mr. Cathcart: I will now offer this statement in evidence, if your Honor please, and I want to call particular attention—

The Court: Just a minute, let's give it a number first, before you read any part of it. [159]

Mr. Cathcart: Yes.

The Court: This is a part of another file, so we will receive it by reference.

Mr. Cathcart: It is a statement dated June 24, 1946.

The Clerk: Defendant's Exhibit *C* in evidence.

(Statement referred to above was then received in evidence as Defendant's Exhibit *C*.)

(Testimony of Allan J. Warner.)

DEFENDANT'S EXHIBIT B

San Francisco, Calif.

June 24, 1946

My name is Allen J. Warner age thirty (30) married and live at No. 10 Ord Court, San Francisco, Calif with my wife June age twenty seven (27) and my minor son Richard. I am engaged in the trucking business with Robert W. Woodrow age twenty nine (29) of 1500-Cole Street, San Francisco. We are the co-owners of a 1939 Dodge tractor motor number T78-1665 Serial No. 8702218 and a 1938 Doane Trailer Model No. 115. I have a drivers license and chauffeurs license No. R904798 and No. 423118 respectively current and restricted to wearing adequate glasses. On Saturday June twenty second (22) at about one thirty (1.30) PM I was involved in an accident while operating the above described equipment. My wife June was riding in the cab with me at the time. The accident occurred about two (2) miles south of Scotia, Calif on Highway No. 101). I had no cargo at the time. I was returning from Willow Creek, Calif. I had taken my mother and son there to visit my sister at Willow Creek. On the return trip I was driving south on No. 101 a two lane, paved highway in the right hand lane of travel. I had been going about forty (40) miles per hour. About two (2) miles south of Scotia I was rounding a slight curve angling to the right and as I approached the steel truss bridge at this point I

(Testimony of Allan J. Warner.)

cut my speed to thirty (30) MPH. Then I saw a north bound car approaching on the bridge. There is an expansion joint on either side of the bridge where it joins the highway. These joints are about two (2) feet wide and there is a slight hump to them. It seems they are constructed of planks below and paved over with asphalt. As I drove on the bridge at a slight angle due to the curve in the road the front wheels of my truck left the pavement completely then bounced to the left across the white line and directly in the path of the on-coming or north bound car. We collided just about head on about five feet (5) south of the north bridge approach. The impact pushed the struck car back about five (5) feet. At the time of the impact my left front wheel was over or left of the white line thirty three (33) inches according to measurements taken later by the highway patrol. After the accident I got out of my cab went over to the left door of the struck car which I had trouble in getting open and assisted the driver out. He appeared dazed and started to walk away. I got ahold of him and had him sit down on the left side of his car, then assisted the other occupant a lady out of the car. Her face and head were bleeding and her right leg appeared to be badly injured. She was unconscious when I lifted her from the car. By that time another car approached and I got a blanket and a pillow from the occupant then wrapped the lady in the blanket and put her at the road side. I then requested the driver of

(Testimony of Allan J. Warner.)

another car that then approached the scene to go back to Scotia to notify the Highway Patrol and secure an ambulance. At the scene I learned the injured were Mr. and Mrs. Geo. W. Bolters both about thirty (30) years of age and that he could be reached at the Olympic Hotel at Seattle, Washington. Both were taken to the Scotia Hospital by ambulance that arrived about twenty (20) minutes after the accident. The highway patrol (one officer) made a detailed investigation at the scene. He said my left rear dual wheels skidded twenty seven (27) feet prior to the impact and that the left front wheel of my truck was thirty three (33) inches to the left of the white line. The officer told me that towns people tried several times to have that bridge condemned because of its narrowness. No citations were issued. The tow truck then arrived and towed the struck car to the Scotia Garage. It was either a Buick or Oldsmobile of late model and a coach I believe. My tractor also was towed to the same garage. I then went to the hospital and talked to Mr. Bolters. He said he saw me approach the bridge from about a half block distance and that he was going about thirty (30) MPH and estimated my speed about the same. He said also he was a field engineer for the Chuisse Pump Company of San Francisco and that he was transferred to Seattle and was on his way to his new headquarters. I also saw his wife at the hospital after the leg (right) was placed in a cast. It seems the foot was broken below the ankle. I

(Testimony of Allan J. Warner.)

then had emergency repairs made to my tractor and I drove it back to San Francisco. I nor my wife had any intoxicating liquor to drink prior to the accident and I don't believe the occupants of the other car had been drinking. The weather at the time was clear and dry. I read this statement of four and one half pages (4½). I understand it and it is true.

(s) ALLEN J. WARNER.

The Court: I may state to the jury a fact which I am sure you are familiar with, and that is that any of these documents which are introduced in evidence, you are entitled to have sent out to you if you so desire. You just call for the exhibits, and all of them will be sent to you so that you can examine them. Counsel may not wish to take time to read it all, or read them all to you, because they are interested in only certain portions, but you have a right to see the document and read it in its entirety, because it is part of the record of the case. All you do is to ask for the exhibits, after you retire to the jury room.

Mr. Cathcart: Now the statement reads in part—this has been admitted in evidence, your Honor?

The Court: Yes, it has been received.

Mr. Cathcart: Q. This statement is the report of the accident that you made to your insurance company, isn't it? A. That's right.

Q. And it reads in part, and of course Mr. Gray can go to any [160] other parts of it that are pertinent: (Reading)

(Testimony of Allan J. Warner.)

“ . . . The accident occurred about two (2) miles south of Scotia, Calif., on Highway No. 101. I had no cargo at the time. I was returning from Willow Creek, Calif. I had taken my mother and son there to visit my sister at Willow Creek. On the return trip I was driving south on No. 101, a two lane paved highway, in the right hand lane of travel.”

And then it goes into the facts of the accident.

Mr. Cathcart: Q. Now is that the report that you gave the insurance company?

A. That's right.

Q. Yes. And now—

Mr. Gray: May I have that?

Mr. Cathcart: Surely.

Q. Now these other matters that you recalled, after you gave the first reports—that is, this report of course, we have just read, and it doesn't refer to any cargo of any kind, to any functions of that kind on your trip north. Now when did it first occur to you that those things were important?

A. Well after talking to truck owners.

Q. What did truck owners say?

A. The truck owners told me that I should have mentioned my cargo.

Q. So after that, you did? [161]

A. After that, I did.

Q. Well now, you talked about—

The Court: Just a moment, let me ask you this:

Q. Did they tell you why?

A. No, they didn't tell me why.

(Testimony of Allan J. Warner.)

Q. They didn't tell you why at all?

A. No, they didn't.

Q. Well, I suppose you thought you were covered right up until when?

A. Right up until I wasn't.

Q. When what?

A. Well, I don't know just exactly when.

Mr. Cathcart: Q. Well, did you ever get any communication from Mr. Gray which suggested that there might be some question about coverage?

A. No, I don't think so.

Q. Well, I will show you a copy of a letter received by our office, dated December 4, 1946, on the stationery of Mr. Gray, addressed to you and Robert Woodrow, with copies to our office. I may say that the copies indicated were sent to Cooley, Crowely, Gaither & Dana, our predecessors in this representation.

Mr. Gray: Counsel, I will stipulate that you may put that entire letter into evidence, and that it was duly mailed to Warner and Woodrow.

Mr. Cathcart: All right. [162]

Mr. Gray: And I will stipulate that you may put the letter in evidence.

The Court: However, as to that stipulation, the question which Mr. Cathcart is asking is as to whether the original was received by this witness. If you can cover that by stipulation, then it will be complete.

Mr. Gray: Well of course he isn't my witness, and I don't know. You can ask him.

(Testimony of Allan J. Warner.)

The Court: But you wrote him the letter.

Mr. Gray: I wrote the letter, and it was put in the mail, and there was a stamp on it. So he should have received it.

The Court: All right, ask him.

Mr. Cathcart: Q. Did you receive this letter?
(Indicating)

The Court: You mean the original of this letter, of course.

(Document handed to witness.)

A. I heard something about this, but I have never seen it myself.

Q. You heard something about this letter. Well, whom did you hear about this letter from?

A. I believe from my mother.

Q. Well, did she tell you that the letter had arrived?
A. Yes.

Q. And I suppose she told you what was in it, more or less?
A. No, she didn't. [163]

Q. What did you say?

A. I believe the letter is still unopened at home.

Q. The letter from Mr. Gray addressed to you is still unopened?

A. That's right. I believe it is.

The Court: All right.

Mr. Cathcart: Q. Well, would it be there today, do you suppose?

A. I don't know whether it would or not. I was out of town at that particular time, when the letter arrived. I had been out of town for about two months and when I came back, I figured it was of

(Testimony of Allan J. Warner.)

no importance then, it wouldn't have done any good anyway.

Q. Well it was dated December 4, 1946; do you recall when you received it, or when you first saw it or first heard of it?

A. About two months later.

Q. You first heard of it around February of 1947, is that correct? A. I don't know.

Q. Well what did your mother say, that there was a letter for you from Mr. Gray?

A. That there was a letter from Mr. Gray, yes. But as I understood it, I was to get in touch with Mr.—with my insurance company, the way I have always understood it. I understood that I was to get in touch with my insurance company, [164] and they were to handle all matters of any paper or letters or anything like that coming from another attorney.

Q. I see. Did you send it to your insurance company? A. I don't believe I did.

Q. And you did not open it?

A. No, I didn't.

Q. And as far as you know, it is there to this day? A. I imagine it is.

Mr. Cathcart: Well, if your Honor please, we will offer this letter in evidence and let the jury determine whether or not this witness, perhaps, read it and closed it up and forgot about it. I mean, I am not suggesting any bad faith.

Mr. Gray: No objection to the letter going in evidence.

(Testimony of Allan J. Warner.)

The Court: All right, it may be received.

The Clerk: Defendant's Exhibit C in evidence.

(The letter was received and marked Defendant's Exhibit C.)

DEFENDANT'S EXHIBIT C

(Copy)

Nathan G. Gray
Attorney At Law
American Trust Building
Berkeley 4, California
BERkeley 6161

December 4, 1946

Messrs. Allen J. Warner
and Robert W. Woodrow
10 Ord Court
San Francisco, Calif.

Gentlemen:

I have received a copy of a complaint from which it appears than an action has been commenced against you by Commercial Standard Insurance Company in the United States District Court for the Northern District of California, Southern Division. My clients, George W. Boulter and Margretta L. Boulter, are also named as defendants in this action.

Normally it is improper for an attorney to address a communication to the adverse parties when they are represented by attorneys as you are. However, this is not a normal case, in that while you

(Testimony of Allan J. Warner.)

are adverse parties in the case brought against you by George W. Boulter and Margretta L. Boulter in the Superior Court in San Francisco, there is a unity of interest between us in the action brought in the United States District Court. To make the situation more anomalous, you are being defended in our action in the Superior Court by the same firm that is suing you in the United States District Court, and both matters pertain substantially to the same subject matter.

In other words, insofar as the United States District Court action is concerned, it is to our advantage for you to prevail, in that it makes available money for the settlement of any judgment that we may be accorded in the Superior Court, whereas from your standpoint it relieves you from the expense of defending the action and paying the judgment against you if one is obtained, in an amount not exceeding the limits of your insurance policy.

My reason for taking the liberty to write to you and explain this matter is merely in the hope that it will result in your taking proper steps to defend this action, and if you have already placed this District Court matter in the hands of an attorney, it would be greatly appreciated if you would turn this letter over to him with the request that he communicate with me.

Very truly yours,

NATHAN G. GRAY,

NGG:FLR

(Testimony of Allan J. Warner.)

CC: Messrs. Cooley, Crowley, Gaither & Dana, Attorneys at Law, 206 Sansome Street, San Francisco, California.

Mr. Cathcart: Q. Well, you finally did hear that there was some pretty grave question about whether you were covered in this accident, didn't you? A. That's right.

Q. Do you remember when it was first brought to your attention, when you first heard that?

A. No, I don't; I haven't the least idea.

Q. Well would it be several months after the accident happened? The accident happened on June 22nd, 1946, and there was an action [165] filed in August, 1946. That is when the Boulters sued you. That is in the answer here. And that finally didn't get to trial until almost a year later, October 27, 1947. Had you heard about it up to that time?

A. I don't know.

Q. You don't know?

A. No, I don't know.

Q. Well, do you recall when you testified before Judge Goodman? A. No, I don't.

Q. Well, all right. But it was after you heard that there was a possibility of there being no coverage that you realized the importance of your activity on that trip, is that correct?

A. That's correct.

Q. And that was after the truck drivers had talked to you? A. That's right.

Q. All right, I see.

Mr. Cathcart: I think that is all.

Mr. Gray: All right, Mr. Warner.

(Witness excused.)

Mr. Gray: Before I forget it, your Honor, I would like to offer in evidence Mr. Warner's testimony before Judge Deasy, as long as the witness has testified about it, and as long as we have the testimony before Judge Goodman. May that be in evidence?

The Court: I beg your pardon? [166]

Mr. Gray: May I offer in evidence the transcript of the testimony of Mr. Warner before Judge Deasy?

The Court: With a jury case, we can't receive it, because we don't send the transcript in. You will have to read what you want.

Mr. Gray: Well I mean, I will read it here.

The Court: Well, the only thing is that we never do that—we never send a transcript of testimony out to the jury.

Mr. Gray: Well, you just put the transcript of Judge Goodman's proceedings, the testimony in; I want to do the same thing.

The Court: No, it was read.

Mr. Cathcart: Just a part of it was read.

The Court: Yes, a portion of it was read. The only way you can do that with a jury is to read it, or, you could give it a mark of identification, and then the portions you want, you can read, because we don't send the transcripts out to the jury. I am sure that is the rule here. It is the rule of California.

Mr. Gray: Could we take out that portion that refers to this matter?

The Court: No, no testimony is ever sent out to a jury. I am sure that is the rule here, gentlemen, because I have been practising law in California for a long time. I don't [167] want to give away my age, but it would be nearly 40 years, and 21 have been as a judge. I don't know of any rule that allows testimony to be given to the jury. In fact, we have a rule that if the jury desires to hear part of the testimony, we read from the transcript to them ourself. I spent four hours with a jury one Sunday reading a testimony. I preferred to read it myself.

Mr. Gray: Well, it wasn't intended as testimony, it was just as prior contradictory statement, and I wanted to show—

The Court: Well, then, you read it to them—read it to the jury and I will have the Clerk identify it as an Exhibit. He will be in in a minute. I am sorry, gentlemen, I mislaid some instructions. The secretary says she wrote them up and I can't find them.

Mr. Gray: I will read all that is relevant.

The Court: Are you through with him?

Mr. Gray: No, there are some questions I want to ask him.

The Court: All right, have him step down. He might be more comfortable.

Mr. Gray: Do you mind staying there?

Mr. Warner: I don't care.

Mr. Gray: All right.

The Court: You go ahead?

Mr. Cathcart: What are you reading now, counsel? [168]

Mr. Gray: Wait until I find it.

I just didn't want to have the jury take part of the record with them and not the rest of it.

The Court: I would prefer that you read it into the record. I don't want the jurors to begin arguing about testimony. We don't do that.

Mr. Gray: All right, I will start at the bottom of page 4, line 21, counsel.

Mr. Cathcart: Now excuse me, I want to get on the track of it here. I want to make an objection to any part of this testimony in the Superior Court action that hasn't any bearing on the issues here.

Mr. Gray: Well, I am trying to confine it to the nature of the trip and so forth. If you want to make a suggestion as to where I should start, I will follow your suggestion.

The Court: Well we are interested only in the purpose of the trip.

Mr. Gray: That's right. Well I am trying to do that. I am starting, I think, at a logical point. If I am wrong, why you correct me, counsel. (Reading.)

"Q. Mr. Warner, I call your attention to June 22, 1946, Where did you reside then?

"A. I resided—you mean my residence?

"Q. Yes.

"A. I live at number 10 Ord Street. [169]

"Q. In San Francisco? A. That's right.

“Q. What was your business on that day?

“A. I was in the transportation business.

“Q. What was the name of that business?

“A. It had no name.

“Q. Who was the owner of the business.

“A. My partner and myself.

“Q. And what was your partner’s name?

“A. Mr. Robert W. Woodrow.

“Q. And what is his address?

“Mr. Smith: At the present time?

“Mr. Gray: Yes, now, if you know?

“A. I don’t know.

“Mr. Gray: Q. What was his address on that day?

“A. I am not positive about it. It was on Cole Street. It is Cole and—I am not sure.

“Q. All right. What was your place of business?

“A. We operated out of number 10 Ord Street.

“Q. At your residence? A. That’s right.

“Q. And you say your business was the transportation business? A. That’s right.

“Q. What were you transporting? [170]

“A. General freight of all types, everywhere.

“Q. For hire? A. That’s right.

“Q. You would haul anything for a certain stipulated rate? A. That’s right.

“Q. And how many trucks or pieces of equipment did you have?

“A. At one time or at that time?

“Q. At that time? A. One.

“Q. And was that the vehicle involved in this accident? A. That is the one.

“Q. Well, now, what was Mr. Woodrow’s work in connection with this partnership?

“A. About the same as mine.

“Q. He would drive the truck or tractor the same as you would? A. That’s right.

“Q. And you were partners with each other?

“A. That’s right.

“Q. What was the type of equipment?

“A. It was a 1939 Dodge 2½ ton tractor.

“Q. And was that the device that is used to hook a trailer onto? [171]

“A. That’s right. It was what is known as a tractor-trailer combination.

“Q. And did you at that time have a trailer to go onto it?

“A. I had a trailer to go onto it at Eureka that belonged onto it.

“Q. To be put on there? A. That’s right.

“Q. Now, calling your attention to the date of the accident, June 22, 1946, you were driving this Dodge truck, is that correct?

“A. That’s right.

“Q. In what direction were you going?

“A. I was headed south.

“Q. And where had you been?

“A. I had been to Blue Lake.

“Q. And that is in Lake County, is it?

“A. That is in Lake County.”

We know that is not correct.

“Q. Had you left what you call the device in the back of the trailer? A. The trailer.

“Q. Had you transferred the trailer up there?

“A. I had taken the trailer up with a load of pipe.

“Q. Where had you taken it?

“A. To Blue Lake. [172]

“Q. From where?

“A. From San Francisco.

“Q. From what company?

“A. For no company, for a relative that had a summer home up there.

“Q. You transported pipe for a relative?

“A. That's right.

“Q. Were you ever paid for it?

“A. Yes, I got \$75 for the haul.

“Q. And you brought the pipe to Lake County?

“A. That's right.

“Q. And you left the trailer there?

“A. That's right.

“Q. With the pipe on it?

“A. No, the pipe had been taken off.

“Q. Well, what was your destination at the time of the accident?

“A. I was on my way back to San Francisco.

“Q. Did you intend to come back to get the trailer? A. I did.

“Q. You eventually did go back to get the trailer? A. I did.

“Q. And when did you do that?

“A. About five days later.

“Q. Was anybody travelling with you? [173]

“A. No, the second trip, no.

“Q. At the time of the accident?

“A. At the time of the accident, my wife was with me.

“Q. What is her name?”

And I think that should be June Warner.

“Q. Is she in Court? A. No.

“Q. Where does she live?

“A. Number 10 Ord Street.”

Mr. Cathcart: “Ord Court”, I have here.

Mr. Gray: I am sorry. “Ord Court.”

Mr. Gray: (Reading.)

“Q. Your wife had been with you since the time you started? A. No.

“Q. Did you take her with you?

“A. She had been up there on vacation.

“Q. She was in Lake County?

“A. That’s right.

“Q. Let’s see if we can get the facts right. Your wife was at Blue Lake, Lake County, and you were in San Francisco, is that right?

“A. That’s right.

“Q. And a relative of yours ordered the pipe taken up and you agreed to transport the pipe to Lake County for this [174] relative for a certain sum of money, is that right? A. That’s right.

“Q. You were paid that money?

“A. That’s right.

“Q. That went into the partnership, is that right? A. That’s right.

“Q. Then you took the trailer and the tractor that were hitched together, and a load of pipe, and went to Lake County from San Francisco, is that right? A. Yes, sir. It is.

“Q. And there you disconnected the tractor and left the pipe—you disconnected the trailer from the tractor and left the pipe in Lake County, is that right? A. That’s right.

“Q. At the time of this accident, you were returning to San Francisco? A. That’s right.

“Q. Were you returning back to continue with your business?

“A. No, I had a definite purpose in coming down, I might state. I had a payment due on my insurance policy Monday. My policy would lapse if I did not get in here Monday. That was the reason for coming down to Frisco here.

“Q. So you came down for that business?

“A. That’s right.

“Q. And when did you intend to go back for your trailer? [175] A. The following day.

“Q. For your trailer?

“A. The following day.

“Q. That would have been Tuesday?

“A. Yes.

“Q. What day did this accident occur?

“A. That happened on a Saturday.

“Q. Now going back to our Dodge tractor, that was registered with the Department of Motor Vehicles, wasn’t it? A. It was what?

“Q. It was registered with the Department of Motor Vehicles, like an automobile? A. Yes.

“Q. And that was registered in your name and Mr. Woodrow’s? A. That’s right.”

And then the rest of it is about the accident. I

guess we are not concerned with that, is that correct?

The Court: Yes, all right.

Mr. Cathcart: Excuse me for one moment, before we leave that subject. Would you stipulate that testimony was given on September 15, 1947, at the trial in a state court action under cross-examination by you?

Mr. Gray: Yes, I have stated that.

Mr. Cathcart: And that was after the testimony before [176] Judge Goodman, which was on August 11, 1947?

Mr. Gray: If those are the dates.

Mr. Cathcart: That is my best information.

Mr. Gray: All right.

Further Recross Examination

Mr. Gray: Q. And now Mr. Warner, counsel has interrogated you about a statement that you gave to an adjuster for the insurance company? Where was that statement taken from you?

A. Some place, I believe it was on Pine Street, I am not sure, though.

Q. Well, it was the office of the company, one of the—

A. No, I don't think it was. I think it was, the way I understand it—I am not positive, but I would say the way I understood it, it was the adjuster of a different place. I am not sure about that.

Q. Well anyway, you were directed by the insurance company to see this man? A. Yes.

Q. And to tell him the facts?

A. Yes. That's right.

Q. And when you saw him, he asked you certain questions, did he? A. That's right.

Q. And you gave him certain answers, is that right? [177] A. That's right.

Q. And then he made certain notes, is that right? A. Yes.

Q. And then he had you sign these notes, is that right? A. That's right.

Q. Now in this statement that counsel called your attention to, there is nothing said about pipe hauling or anything. Did this adjuster ask you whether you had hauled anything up to Willow Creek? A. No, I don't believe he did.

Q. Well—

The Court: We are going over this thing unnecessarily. I asked those questions to avoid your having to do so.

Mr. Gray: Well, counsel went into it, is the reason I am.

The Court: Well I know, but he has given the explanation; he has stated that he never mentioned that to anyone, that he wasn't asked the question, that the only time he began thinking and talking about the load was after he talked to somebody.

Mr. Gray: Other haulers.

The Court: Whatever they call them.

The Witness: Operators.

The Court: Operators, yes, who told him that it was important, is that correct? [178]

The Witness: That's correct.

The Court: All right.

Mr. Gray: Well, then, one question on that.

Q. Do I understand it is your testimony that the only reason that you didn't make mention of pipe or hauling anything was because it wasn't asked, is that correct? A. That's right.

The Court: I am sorry, that is not a correct summary. That is not a correct summary of this testimony.

Mr. Gray: Well I mean, as far as this adjuster is concerned.

The Court: Oh yes, that is correct.

Mr. Gray: Yes.

The Witness: Yes, that is correct.

The Court: All right, go ahead.

Mr. Gray: That is all.

The Court: Q. And you didn't mention it to the others because you didn't think it was important? A. No.

Q. In other words, until you began to think that possibly the omission that the fact that you were carrying pipe was important so far as your coverage is concerned, you just talked about the trip, is that correct? A. That's right.

The Court: All right. Any more questions, gentlemen?

Mr. Cathcart: Do you remember making any statement to [179] your insurance company?

A. No.

Q. You don't recall ever having made any written statement, or a written report about this question of coverage?

A. No, I could have. I wouldn't swear to it.

Q. You wouldn't remember what it could have been?

The Court: Well, if you have anything, just show it to him and save time.

Mr. Cathcart: I don't have the original, I just have a copy. I don't know where the original is.

The Court: Well, is the copy in typewriting?

Mr. Cathcart: Yes sir, it is a typewritten copy. It is not signed.

The Court: It is not signed?

Mr. Cathcart: No, it just has an indication of signature.

A. I can recognize my own words.

Mr. Cathcart: Q. I will ask you to read this.

Mr. Cathcart: I am sorry, I do not have a copy.

Mr. Gray: Well counsel, I think you should show it to me.

Mr. Cathcart: I want to see if this gentleman can recognize it.

Mr. Gray: Well, I would like to know what it is about.

Mr. Cathcart: Surely.

Mr. Gray: No date on it, and no signature.

Mr. Cathcart: I just want to ask him.

The Court: Well counsel, I was the one who suggested that he might show it to him. If the witness cannot identify it—

Mr. Gray: Well, if he offers it—

The Court: You may insist on the proper foundation being laid. All he is trying to do is to find out.

(Document handed to witness.)

The Court: I am trying to come to a stopping point, ladies and gentlemen of the jury, and I will give you a recess. Probably we will excuse you for the morning while we go on and attend to other matters.

The Court: Q. Does that read like something you said to them later on after that statement?

A. Certain parts of it I would say are my words, but there are other parts that are not my words.

The Court: Well all right then; that wouldn't be sufficient foundation.

Mr. Gray: No.

Mr. Cathcart: No sir.

The Court: Anything further?

Mr. Cathcart: No sir.

Mr. Gray: That is all.

The Court: All right.

(Witness excused.) [181]

The Court: All right, gentlemen, do you have anything else?

Mr. Gray: Are you finished with Mr. Warner?

Mr. Cathcart: Yes sir.

Mr. Gray: You may be excused.

The Court: All right. Well now, gentlemen, let's have an understanding; does that close the testimony in its entirety?

Mr. Gray: Yes, your Honor.

Mr. Cathcart: Yes sir.

* * * *

[182]

Mr. Cathcart: Well then, I at this time will renew my motion for a directed verdict in favor of defendant, on all of the grounds stated yesterday.

That will be the ruling of the Court. I shall reserve the ruling on the motion for directed verdict until after the verdict, under the provisions of Section 50(b) of the Federal Rules of Civil Procedures.

CERTIFICATE OF REPORTER

I, Eldon N. Rich, Official Reporter, *protem*, certify that the foregoing 186 pages is a true and correct transcript of the matter therein contained as reported by me and thereafter reduced to typewriting to the best of my ability.

[Endorsed]: Filed Oct. 5, 1948.

[186]

[Endorsed]: No. 12056. United States Court of Appeals for the Ninth Circuit. George W. Boulter and Margretta L. Boulter, Appellants, vs. Commercial Standard Insurance Company, a corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed October 5, 1948.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

In the United States Court of Appeals for the
Ninth Circuit

No. 12056

GEORGE L. BOULTER and MARGRETTA L.
BOULTER,

Plaintiffs and Appellants,
vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,
Defendant and Appellee.

STATEMENT OF POINTS UPON WHICH
PLAINTIFFS AND APPELLANTS IN-
TEND TO RELY, AND DESIGNATION OF
PARTS OF RECORD NECESSARY FOR
THE CONSIDERATION THEREOF

Following is a statement of the points upon which plaintiffs and appellants intend to rely on the appeal in this cause:

Plaintiffs and appellants do hereby adopt and incorporate by reference herein a statement of the points upon which they intend to rely on the appeal in this cause which was heretofore filed in the office of the clerk of the court from which this appeal is taken.

Plaintiffs and appellants do hereby adopt and incorporate by reference herein the designation of parts of record necessary for the consideration of the points made in the appeal in this cause which was heretofore filed in the office of the clerk of

the court from which this appeal is taken except that only those parts of the reporter's transcript that are hereinafter set forth are deemed necessary by plaintiffs and appellants for a consideration of this appeal:

Page 2, line 6, to page 9, line 12.

Page 10, lines 8 to 25.

Page 28, line 15, to page 65, line 15.

Page 115, line 23, to page 140, line 23.

/s/ NATHAN G. GRAY,
Attorney for Plaintiffs and Appellants, George W.
Boulter and Margretta L. Boulter.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed Oct. 5, 1948. Paul P. O'Brien,
Clerk.

No. 12056

United States
Court of Appeals
for the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Appellee.

SUPPLEMENTAL
Transcript of Record

Appeal from the United States District Court
for the Northern District of California,
Southern Division

In the Superior Court of the State of California,
in and for the City and County of San Francisco

No. 371,020

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Plaintiffs,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant.

NOTICE OF INTENTION TO FILE PETITION
AND BOND FOR REMOVAL OF CAUSE TO
THE UNITED STATES DISTRICT COURT
AND OF MOTION FOR ORDER FOR SUCH
REMOVAL

To George W. Boulter and Margretta L. Boulter,
Plaintiffs Above Named, and to Nathan G. Gray,
Attorney for Said Plaintiffs:

You and Each of You Will Hereby Take Notice
that the above named defendant, Commercial Stand-
ard Insurance Company, by its attorneys, Dana,
Bledsoe & Smith, will on Friday, the 19th day of De-
cember, 1947, at the hour of 3:15 o'clock p.m. of said
day, file in the above entitled court its verified peti-
tion and bond for removal of this cause from the
said Court to the District Court of the United States
for the Northern District of California, Southern
Division; a copy of each of said documents is here-
unto annexed.

You Are Further Notified that the said defendant,
by its attorneys, will on said 19th day of December,

1947, at the hour of 3:15 o'clock p.m., or as soon thereafter as counsel may be heard, at the courtroom of the above entitled court, in the County Court House, in the City and County of San Francisco, State of California, move the said court for an order approving the said verified petition and bond and removing this cause to the District Court of the United States for the Northern District of California, Southern Division, and directing the Clerk of said State Court to make up the record in said cause for transmission to said District Court.

Said motion will be based and heard upon the said verified petition and bond for removal of said cause, and will be made upon the grounds of the diversity of citizenship as appears from the said verified petition, and upon the propriety and sufficiency of the proceedings herein taken to effect such removal under the Federal Judicial Code.

Dated: December 18, 1947.

DANA, BLEDSOE & SMITH,
Attorneys for Defendant.

[Endorsed]: Filed Dec. 19, 1947.

[Title of Superior Court and Cause.]

PETITION FOR REMOVAL OF CAUSE TO
THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALI-
FORNIA, SOUTHERN DIVISION

To the Honorable Superior Court of the State of
California, in and for the City and County of
San Francisco:

Petitioner appears herein especially for the sole purpose of this petition and not otherwise and such special appearance shall not be deemed to be a general appearance or a submission to the jurisdiction of this court to which your petitioner specifically reserves the right to object.

The petition of Commercial Standard Insurance Company respectfully shows:

I.

The above entitled action has been brought in this court and is now pending therein; the complaint in the above-entitled action was filed and summons was issued on November 19, 1947; your petitioner was served with a copy of said summons and complaint in the City and County of San Francisco, State of California, on December 10, 1947; the time within which said defendant is required to answer or otherwise plead has not yet expired.

II.

Said action is of a civil nature, arising from a judgment obtained by plaintiffs in a personal injury action against two defendants alleged to have been

insureds of your petitioner and this suit is upon an insurance policy issued by defendant petitioner.

III.

That the value of the matter in controversy exceeds the sum of \$3,000.00 exclusive of interests and costs; that plaintiffs pray for damages in the sum of \$5,118.76, together with interest thereon.

IV.

That at all times mentioned in said complaint and **at the time said action was commenced, and at all times since, and at the present time,** the defendant Commercial Standard Insurance Company, your petitioner, was and is a corporation duly organized and existing under and by virtue of the laws of the State of Texas; that at all times hereinabove mentioned said defendant, your petitioner was and is a citizen of the State of Texas; that plaintiffs at the commencement of this action were and at all times since have been citizens of the State of Oregon.

V.

Your petitioner has heretofore given notice to the plaintiffs of the filing of this petition and the bond for removal hereinafter mentioned.

VI.

Your petitioner presents herewith a good and sufficient bond as provided by the statute in such cases made and provided, that it will enter into the District Court of the United States for the Northern District of California, Southern Division, within thirty (30) days from the date of the filing of this

petition a certified copy of the record in this suit, and that it will pay all costs which may be awarded by the District Court in the event that the said court shall decide that this action was wrongfully or improperly removed thereto.

Wherefore, your petitioner prays that this court proceed no further herein except to order the removal, accept the bond herewith presented and direct a transcript of the record to be made for filing in the United States District Court aforesaid.

Dated: December 18, 1947.

DANA, BLEDSOE & SMITH,
Attorneys for Defendant.

(Duly Verified.)

[Endorsed]: Filed Dec. 19, 1947.

[Title of Superior Court and Cause.]

MEMORANDUM OF POINTS AND AUTHORITIES
IN SUPPORT OF PETITION FOR RE-
MOVAL OF CAUSE TO DISTRICT COURT
OF THE UNITED STATES

I.

Duty of Court to Accept Petition Together with Bond and Order of Removal.

“It shall be the duty of said court to accept said petition and bond and proceed no further in such suit.”

Judicial Code, Sec. 29, U.S.C.A. Title 28, Sec. 72, p. 395.

II.

The Controversy is Wholly Between Citizens of Different States and Petitioner is Entitled to Removal of Cause.

Judicial Code, Sec. 28, U.S.C.A. Title 28, Sec. 71, p. 3.

Respectfully submitted,

DANA, BLEDSOE & SMITH,
Attorneys for Petitioner-Defendant.

[Title of Superior Court and Cause.]

BOND ON REMOVAL

Know All Men By These Presents:

That Commercial Standard Insurance Company, a corporation organized and existing under and by virtue of the laws of the State of Texas, defendant in the above entitled suit, as Principal, and American Surety Company of New York, a corporation organized under the laws of the State of New York, as Surety, are held and firmly bound unto George W. Boulter and Margretta L. Boulter, plaintiffs above named, in the sum of Five Hundred and No/100 Dollars (\$500.00), lawful money of the United States for the payment whereof, well and truly to be made, we hereby bind ourselves, our successors, representatives and assigns, jointly and severally by these presents.

The Condition of This Obligation is Such, that whereas the said Principal has filed, or is about to file, its petition in the Superior Court of the State

of California, in and for the City and County of San Francisco, praying for the removal of a certain cause pending therein, as above entitled, wherein George W. Boulter and Margretta L. Boulter are the Plaintiffs, and the said Principal is defendant, to the Southern Division of the District Court of the United States for the Northern District of California;

Now, Therefore, if the said Principal shall enter in said District Court of the United States, within thirty (30) days from the filing of said petition for removal, a certified copy of the record in said suit, and also shall appear therein, and shall and truly pay all costs that may be awarded by the said District Court if said District Court shall hold that such suit was wrongfully or improperly removed thereto, then this obligation shall be void; otherwise it shall remain in full force and virtue.

In Witness Whereof, the said Commercial Standard Insurance Company, and the American Surety Company of New York have caused these presents to be executed this 18th day of December, 1947.

COMMERCIAL STANDARD INSURANCE COMPANY,

By DANA, BLEDSOE & SMITH,
Its Attorneys.

(Seal) AMERICAN SURETY COMPANY
OF NEW YORK,

By /s/ L. T. PLATT,
Res. Vice-Pres.

Attest:

/s/ M. L. BERTETTA,
Res. Asst. Secty.

Bond No. 35-472-233.

Premium \$10.00 per annum.

Approved:

GEORGE W. SCHOENFELD,
Presiding Judge of the Superior Court
Dec. 19, 1947.

[Affidavit of Service by Mail attached.]

[Endorsed]: Filed Dec. 19, 1947.

[Title of Superior Court and Cause.]

ORDER FOR REMOVAL OF CAUSE

This cause coming on for hearing upon the petition and bond of the defendant, Commercial Standard Insurance Company, herein, for an order transferring this case to the United States District Court for the Northern District of California, Southern Division, and it appearing to the court that the defendant, Commercial Standard Insurance Company, has given plaintiffs due and legal notice thereof;

And it appearing to the Court that this is a proper cause for removal to said District Court:

Now Therefore, said Petition and bond are hereby accepted, and it is hereby ordered and adjudged that this cause be and is hereby removed to the United

States District Court for the Northern District of California, Southern Division, and the Clerk is hereby directed to make up the record in said cause for transmission to said court forthwith.

Done in Open Court this 19th day of December, 1947.

GEORGE Q. SCHOENFELD,
Judge of the Superior Court.

[Endorsed]: Filed Dec. 19, 1947.

Filed Jan. 16, 1948. C. W. Calbreath, Clerk.

In the District Court of the United States, for the
Northern District of California, Southern
Division

No. 27,857-R

GEORGE W. BOULTER and MARGRETTA L.
BOULTER,

Plaintiffs and Appellants,
vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Defendant and Respondent.

REQUEST FOR SUPPLEMENTAL RECORD.
AND DESIGNATED PARTS OF RECORD
TO BE INCLUDED THEREIN

The plaintiffs and appellants above named do hereby respectfully request that the above entitled court make an order that a supplemental record

shall be certified and transmitted by the clerk of this court to the clerk of the United States Circuit Court of Appeals for the Ninth Circuit, and plaintiffs and appellants hereby designate the following parts of the record which they deem necessary to be added to the record heretofore made up for the consideration of the points made in the appeal of this cause:

1. Judgment entered on July 9, 1948, on the verdict of the jury.
2. Petition for removal of cause to the United States District Court for the Northern District of California, Southern Division.
3. Notice of intention to file petition and bond for removal of cause to the United States District Court, and of motion for order for such removal.
4. Bond referred to in the foregoing notice.
5. Order for removal of cause.

Dated: December 17, 1948.

NATHAN G. GRAY,
Attorneys for Plaintiffs and Appellants, George W.
Boulter and Margretta L. Boulter.

The clerk of this court is hereby directed that a supplemental record of the above described documents be certified by him and transmitted to the clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: December 17, 1948.

/s/ MICHAEL J. ROCHE,
Judge of said United States District Court.

[Endorsed]: Filed Dec. 17, 1948.

District Court of the United States
Northern District of California

CERTIFICATE OF CLERK

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 14 pages, numbered from 1 to 14, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of George W. Boulter, et al., Plaintiffs, vs. Commercial Standard Insurance Company, a corporation, Defendant, No. 27857-R, as the same now remain on file and of record in my office.

I, further certify that the cost of preparing and certifying the foregoing Supplemental transcript of record on appeal is the sum of \$1.40, and that the said amount has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 17th day of December, A.D. 1948.

(Seal)

C. W. CALBREATH,
Clerk.

[Endorsed]: No. 12056. United States Court of Appeals for the Ninth Circuit. George W. Boulter and Margretta L. Boulter, Appellants, vs. Commercial Standard Insurance Company, a corporation, Appellee. Supplemental Transcript of Record. Upon Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed December 17, 1948.

/s/PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the
Ninth Circuit.

No. 12,056

IN THE

United States Court of Appeals
For the Ninth Circuit

GEORGE W. BOULTER and
MARGRETTA L. BOULTER,
Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation, *Appellee.*

Appeal from the United States District Court for the Northern District of California, Southern Division.

BRIEF FOR APPELLANTS.

NATHAN G. GRAY,
American Trust Building, Berkeley 4, California,
Attorney for Appellants.

FILED

JAN 10 1949

PAUL P. O'BRIEN,
CLERK

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No. 12,056

IN THE

**United States Court of Appeals
For the Ninth Circuit**

GEORGE W. BOULTER and MARGRETTA L. BOULTER, vs. COMMERCIAL STANDARD INSURANCE COMPANY, a corporation,	<i>Appellants,</i> <i>Appellee.</i>
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Appeal from the United States District Court for the
Northern District of California, Southern Division.

BRIEF FOR APPELLANTS.

The parties herein will be referred to by their designations in the District Court, viz., appellants as "plaintiffs" and appellee as "defendant". Reference to the printed Transcript of Record will be indicated by the letter "T." followed by page number.

PRELIMINARY STATEMENT.

Defendant insurance company issued to its insured an automobile public liability policy. Plaintiffs recovered a final judgment in a state court against its

insured for injuries received in an accident with a vehicle covered by the policy. The instant action was commenced in a state court and removed to and tried in the District Court because of diversity of citizenship. Judgment was entered for plaintiffs upon a jury's verdict, after which the District Court granted a motion for a directed verdict pursuant to a reservation of ruling thereon, and judgment was thereupon entered in favor of defendant. This appeal is from said order and said judgment.

STATEMENT OF PLEADINGS AND FACTS DISCLOSING JURISDICTION.

The complaint was filed in the Superior Court of the State of California in and for the City and County of San Francisco (T. 2). In it plaintiffs seek judgment against defendant for the aggregate amount of \$5,118.76 and interest pursuant to the provisions of an automobile indemnity insurance policy executed by defendant.

Prior to the time in which the defendant was required by the laws of the state or the rules of the court in which said action was brought to answer or plead to said complaint, it filed in the State Court its verified petition for removal of cause to the United States District Court for the Northern District of California, Southern Division (T. 205), notice of intention to file petition and bond for removal of cause to the United States District Court and of motion for order for such removal, which notice was duly served

on plaintiffs (T. 203), and bond referred to in the foregoing notice (T. 208) (28 U.S.C.A. Sec. 72). Thereafter and pursuant to said notice an order was duly given and made by said Superior Court ordering the removal of said cause to said District Court (T. 210).

Said petition discloses that the plaintiffs are residents of the State of California, and that the defendant is a corporation duly organized and existing under the laws of the State of Texas; that the controversy is wholly between citizens of different states and which can be fully determined as between them (28 U.S.C.A. Sec. 71); and that the matter in controversy exceeds, exclusive of interest and costs, the sum or value of \$3,000 (28 U.S.C.A. Sec. 41 (1)).

After the case was removed to the District Court defendant filed its answer therein (T. 9), plaintiffs demanded a jury (T. 43) and the cause was tried before a jury. The verdict of the jury awarding to plaintiffs the amounts prayed for in the complaint was returned and filed on July 7, 1948 (T. 47), and judgment was entered on said verdict on July 9, 1948 (T. 47a).

On July 12, 1948, there was filed a motion of defendant for a judgment notwithstanding the verdict and in the alternative for a new trial (T. 48), and on July 26, 1948, a decision and order were made by the District Court that the motion of the defendant for a directed verdict, on which ruling had been reserved, be granted, that the verdict and judgment for the plaintiffs be set aside, and that judgment be entered

for the defendant that plaintiffs take nothing by their complaint, and that the motion for new trial be denied (T. 51-52). Pursuant to and in accordance with said decision and order, judgment was signed and filed on August 5, 1948, and entered on August 6, 1948 (T. 75).

Notice of appeal to the United States Court of Appeals for the Ninth Circuit, appealing from said decision and order and from said final judgment, was filed by plaintiffs with the District Court on August 18, 1948 (T. 77). An appeal from said order and judgment to the Circuit Court of Appeals is provided by 28 U.S.C.A., Section 225, and said appeal was perfected within the time limit provided by 28 U.S.C.A., Section 230, and by Section 732 of the Rules of Federal Procedure.

STATEMENT OF THE CASE.

The Pleadings.

In their complaint (T. 2) plaintiffs seek to recover from defendant on an automobile public liability policy issued by it to one Warner and Woodrow pursuant to California Highway Carriers' Act, Sections 5 and 6, Deering's California General Laws, Act 5129a. It is alleged therein that plaintiffs were injured by a tractor owned and operated by Warner and Woodrow that was covered by said policy and while it was in effect, and that a judgment for the damages arising therefrom was recovered by plaintiffs against Warner and Woodrow in the State Court; and that the judgment has become final and is wholly unsatisfied.

The material allegations of the complaint are established by the admissions in the answer (T. 9), request for admission of facts (T. 44), statement of defendant, Commercial Standard Insurance Company, in reply to plaintiffs' request for admission of facts (T. 45), oral stipulation during trial (T. 94), and the uncontradicted testimony of Noel Coleman, assistant secretary of California Public Utilities Commission (T. 82-93). The answer, however, pleads several affirmative defenses which present the only controversial issues here involved. A copy of the policy is attached to the answer (T. 25), from which, however, a relevant endorsement was inadvertently omitted (T. 44-45; 86-92).

With the exception of paragraph VII of the answer (T. 13-21), which was stricken out by the court (T. 98-99), and the allegation that the policy did not cover the tractor while it was separated from the trailer (T. 4), which defense was not urged nor considered by the trial court (see Declaration 6 of policy (T. 25)), the defense is based solely on the following provision of the policy, which is set forth in the answer:

“The Automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation”.

The allegations based on this provision are that at the time of the accident Warner, who was then driving, was not operating the tractor under authority of the Highway Carriers' Act, nor was he using it for the

transportation of merchandise, but on the contrary it was being used in violation of the above quoted provision, to-wit: for the purpose of transporting himself and his family on a vacation trip, and for the purpose of carrying himself and his wife home from such trip, and for pleasure purposes of himself and his wife (T. 11-13).

The Trial.

A jury was demanded by plaintiffs, and the case was tried by jury (T. 43). After establishing the facts alleged in their complaint by admissions in the pleadings, testimony of Noel Coleman, and the stipulation referred to above, plaintiffs rested (T. 94). The defendant thereupon moved for a dismissal under Section 41b of the Federal Rules of Civil Procedure on the ground that the plaintiffs did not meet the defense raised in the answer and prove that at the time of the accident the assured was engaged in the transportation of merchandise (T. 95-96). The Court ruled that the plaintiffs had established a *prima facie* case, and denied the motion (T. 96-97).

Defendant thereupon called its assured, Allen J. Warner, as its witness (T. 100), and so far as it is revelant to the issues here involved, and without attempting to reconcile conflicts therein, his testimony on direct examination was substantially as follows:

On June 22, 1946, he was in partnership with Robert W. Woodrow (T. 100), and they were engaged in the transportation of property for hire (T. 101). In this business he used a Dodge tractor and trailer (T. 101), and he operated out of 10 Ord Court, San

Francisco (T. 102). He had no definite route; he wild-catted, which means that he has no definite over-the-road operation of his own, so he subhauls for big contractors (T. 103). On June 22, 1946, he was involved in an accident with the Dodge tractor about two miles south of Scotia in Humboldt County (T. 103-104). He was returning with his wife to San Francisco after leaving the trailer at Blue Lakes (T. 105). He had gone to Blue Lakes a week prior with the trailer, and he was taking 700 feet of pipe and a load of furniture to his sister, for which he was paid (T. 106). He left the pipe and trailer at Willow Creek, and headed back to San Francisco with the tractor, it having been his intention to get a load out of Willow Creek for San Francisco, but there was nothing then coming out of that territory (T. 107). His sister lives there, and at the time he took the lumber, pipe and furniture up he spent his vacation there (T. 109). When he left the trailer, it had not as yet been unloaded (T. 110), and his purpose for returning to San Francisco was to pay an instalment due on the policy in question. It was on this trip that the accident to plaintiffs occurred (T. 111). While he was at Willow Creek he had solicited business (T. 112-113). After the accident he continued on to San Francisco, paid his premium to the insurance company, had his tractor repaired, and then he returned to Willow Creek for his trailer (T. 114-115). Everything had been unloaded from the trailer, and he came back empty (T. 115). A trip to San Francisco without the trailer would enable him to hasten back to pay the premium on the policy, and he intended to pick up

the trailer later (T. 118). At the time of the accident he was not carrying any load or anything in the tractor (T. 119). On his return to San Francisco with the trailer there was a big range and some other stuff that belonged to his sister, for which he was paid \$64 for transporting (T. 120-121).

His testimony on cross-examination was as follows:

The witness was brought before Judge Goodman at the request of Mr. Bledsoe, one of the attorneys for the defendant herein, at which time he gave certain testimony (T. 123).

“Mr. Bledsoe. Q. This trip was in the nature of a vacation trip for you, wasn't it?

A. It was a combination.

Q. What was the nature of the combination?

A. Business had been very slow about that time of the year and we had gone up into Willow Creek for an outfit up there, California Barrel. We had intended, if possible, to haul barrels out of Willow Creek.

Q. Did you see someone while you were up there about that?

A. No, I did not.

Mr. Gray. Q. Now in this hearing before Judge Goodman, Mr. Warner, did you testify to anything about stoves, pipe, or furniture?

A. No, I didn't.

Q. Nothing was said about that?

A. (Witness nodded in the negative.)

Q. Now this tractor that is in your insurance policy is the same tractor as involved in this accident, is that right?

A. That's right.

Q. Now were you paid for taking this pipe and other material up there?

A. Yes, sir, I was.

Q. How much were you paid?

A. \$75."

(T. 124-125.)

At the time of the accident he was taking the most direct route from Willow Creek back to San Francisco (T. 126), and at the time of the accident he was not on his vacation (T. 127). One of his purposes in returning was to discuss with one Dowdell the hauling of a load (T. 127). He left the articles in the trailer as an accommodation to his sister (T. 128). In wild-catting he frequently leaves his trailer with merchandise to be unloaded while he does something else, and this is a customary and usual thing (T. 129). Wild-catting means that he frequently takes his equipment and goes from place to place and hauls for whoever will hire him (T. 138). He does not necessarily start from San Francisco, but from any place where he happens to be where he can locate a job. It is common practice to sometimes take a trailer that is already loaded instead of his own trailer, and attach this to his tractor for some company who has a load, and Dowdell has such trailers (T. 138-139). In wild-catting he has many times used his tractor only for hauling commodities (T. 141).

After the taking of the evidence was concluded, the defendant moved for a directed verdict (T. 198) on all the grounds specified by it on the preceding day, namely: "that it has been shown by evidence that at

the time this accident happened, the vehicle, the Dodge tractor, was not being used for the transportation of merchandise within the meaning of the policy which is in evidence" (T. 136-137). The court reserved its ruling on the motion for directed verdict until after the verdict, under the provisions of Section 50 (b) of the Federal Rules of Civil Procedure (T. 199).

The case was thereafter submitted to the jury, and its verdict was returned in favor of plaintiffs for the amounts prayed for in the complaint (T. 47), and judgment was entered thereon (T. 47a).

Post Trial Proceedings.

Following the entry of judgment defendant filed a written motion for judgment notwithstanding the verdict and in the alternative for a new trial (T. 48). Thereafter the District Court rendered and filed an opinion (T. 53) (78 Fed. Supp. 895), and upon the grounds stated therein the court filed its decision and order that the motion of defendant for a directed verdict, on which ruling had been reserved, be granted; that the verdict and judgment for the plaintiffs be set aside, and that judgment be entered in favor of defendant; and that the motion of defendant for a new trial be denied (T. 51-52). Judgment upon this order was thereupon entered (T. 75). The appeal herein is taken from said order and judgment (T. 77).

Questions Involved.

The judgment here appealed from being one that was entered notwithstanding a verdict of a jury to the contrary, the questions involved are:

1. Did plaintiffs establish a *prima facie* case?
2. Which party had the burden of proving the matters affirmatively pleaded in the answer?
3. Can plaintiffs' *prima facie* case be overcome *as a matter of law* by: any testimony adduced by defendant; or the testimony of one witness called by defendant which the trial court described as a story that is inherently improbable, bearing almost on the fantastic (T. 57)?
4. Did the jury have the right to conclude that the vehicle was being used for transportation of merchandise purposes?

Each of these questions will be discussed in the argument following under appropriate titles.

SPECIFICATION OF ERRORS.

1. The District Court erred in granting the motion of the defendant for a directed verdict, on which ruling had been reserved.
2. The District Court erred in making an order that the verdict and judgment for the plaintiffs be set aside and that judgment be entered for the defendant that plaintiffs take nothing by their complaint.
3. The District Court erred in rendering and causing to be entered a judgment in favor of the defendant that plaintiffs take nothing by their complaint against defendant, that the complaint be dismissed on the

merits, and that defendant recover from plaintiffs its costs of suit.

ARGUMENT.

On June 22, 1946, at the time of the accident here involved, Warner and Woodrow were operating under a Highway Carrier Permit issued by the Railroad Commission of the State of California (T. 83-84), and they were engaged in the business of transporting property for hire (T. 100-101). As a condition for granting this permit they were required to obtain a policy of insurance, and the policy here involved was issued to them (T. 84), and was in full force and effect at the time of the accident (T. 87). One of the declarations in the body of the policy provides:

“5. The Automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation”.

(T. 25.)

This policy was admitted in evidence as plaintiffs' exhibit No. 1 (T. 88). Attached to this policy is an endorsement required by the Railroad Commission (T. 89) which provides:

“* * * that within the classes of coverage provided by the policy it will pay any final judgment rendered against the insured for bodily injuries to or death of any person or persons other than the named insured, or damage to or destruction of property, or both, arising out of the owner-

ship, maintenance or use of any vehicle operated under authority of the aforesaid statutes, although such vehicle may not be specifically described in the policy; that the judgment creditor may maintain an action in any court of competent jurisdiction to compel such payment; that the right of any person, firm or corporation to recover under the policy shall not be affected by any act, omission, or misrepresentation of the insured or his employees with regard to any warranty, condition, declaration, or provision of the policy; and that the policy shall remain in full force and effect notwithstanding such act, omission or misrepresentation or the violation of any warranty, condition, declaration or provision of the policy by the insured or his employees; Provided, However, that this endorsement shall not be construed to impose any obligation on the Company for which it would not be liable independently hereof with respect to * * * (4) any loss arising out of any operations of the insured except operations authorized or for which authorization is required under the aforesaid statutes.

* * *

“The Company further agrees that this endorsement shall prevail over any conflicting provision in the policy or in any other endorsement now or hereafter attached thereto or made a part thereof”.

(T. 89-91.)

The right of the plaintiffs to sue the defendant on the policy is provided by the provisions of the policy itself (T. 39) and by Section 11580 of the Insurance Code of the State of California.

THE PLAINTIFFS ESTABLISHED A PRIMA FACIE CASE.

It would only serve to unnecessarily burden this brief to review the admissions in the pleadings, the evidence, and stipulation of counsel, which together establish every fact alleged in the complaint. Suffice it to say that the case was tried on this theory, which is illustrated by the fact that at the time plaintiffs rested defendant moved for a dismissal under Rule 41b upon the sole ground that to entitle plaintiffs to recover they had the burden of proving that at the time of the accident the tractor was being used only for the transportation of merchandise (T. 95-96). That the allegations of our complaint were established is further illustrated by the statement of the trial court in denying the motion of defendant for dismissal (T. 97).

“So I feel that in this case a prima facie case has been shown when they produce a judgment of the Court in addition to the other facts, which shows a recovery against them for injury caused by their truck and the conditions of liability are general and imposed by statute; the limitation becomes an exception, which it is duty of the defendants to prove.”

(T. 96.)

The effect of *prima facie* evidence and of a *prima facie* case is aptly described in the case of *Miller & Lux Inc. v. Secara*, 193 Cal. 755 (227 P. 171), wherein the Court at pages 770-771 states:

“‘*Prima facie* evidence is that which suffices for the proof of a particular fact until contradicted and overcome by other evidence.’ (Code Civ.

Proc., sec. 1833.) It is to be noted that the code does not say 'until contradicted *or* overcome by other evidence,' but 'until contradicted *and* overcome by other evidence.' Therefore, when *prima facie* evidence of a given fact has been introduced, its effect is not destroyed by the introduction of contradictory evidence. It stands as *proof* of that particular fact unless and until it is *both contradicted and overcome* by such other evidence. 'Proof' is something more than merely 'evidence.' It is 'the establishment of a fact by evidence.' (Code Civ. Proc., sec. 1824.)"

THE DEFENDANT HAD THE BURDEN OF PROVING THAT THE TRACTOR WAS NOT BEING USED FOR TRANSPORTATION OF MERCHANDISE PURPOSES.

Neither the defendant nor the trial judge has at any time questioned the sufficiency of our complaint to state a cause of action, nor the sufficiency of the admissions and evidence to establish its allegations. Hence, the only question remaining on this subject is whether it was incumbent upon plaintiffs to have gone further and negated the affirmative defenses pleaded in the answer. During the trial the District Judge held that this burden was not imposed upon plaintiffs (T. 96), and he does not in his written opinion (T. 53) directly discuss this point except to state:

"It is to be borne in mind that we are interpreting a contract which contains a condition or limitation of liability, regardless of whom has the burden of the proof."

(T. 58.)

In support thereof the learned judge cites *Zohner v. Sierra Nevada L. & C. Co.*, 114 Cal. App. 85, 90, and *Ells v. Order of United etc. Travelers*, 20 Cal. (2d) 290, 304. In the *Zohner* case the rule that we contend was there stated on the page cited.

“It is fundamental that the burden was upon appellant (insurance company) to show that the circumstances brought the case within the exception of the policy and this burden appellant failed to meet.”

The *Ells* case merely reenunciates the familiar rule that in an action on an accident policy it is incumbent upon the person claiming thereunder to establish that the death was caused by accident.

The distinction between the necessity of a plaintiff proving that the death of a decedent was caused by an accident and the necessity of a defendant proving that the death resulted from perils which were excepted risks under the policy appears in the case of *Davilla v. Liberty Life Ins. Co.*, 114 Cal. App. 308 (299 P. 831), wherein the court states:

“The burden of proving that death resulted from the two specified causes, i.e., the risk covered, rested upon respondent. (plaintiff) (p. 313) * * *

“In considering appellant’s (defendant) claim that the evidence establishes, as a matter of law, that insured’s death was ‘contributed to or caused by voluntary exposure to unnecessary danger’ and occurred ‘while violating the law’, it must be remembered that these perils were excepted risks as to which appellant had the burden of proof.” (p. 317).

In *Zenner v. Goetz*, 324 Pa. 432, 188 A. 124, the defendant insurance company claimed that after a verdict and judgment for plaintiffs its motion n. o. v. should have been granted, in that testimony offered by it established that the insured was carrying passengers for compensation contrary to the provisions of the policy.

“At the trial appellant’s defense was that defendant at the time of the accident was transporting passengers for compensation and consequently his insurance policy did not cover the liability assumed by the company. It contended, then as now, that to recover against it, plaintiff was required to show compliance by defendant with all the terms of his policy, including the fact that when the accident occurred the latter was not engaged in carrying passengers for hire. Plaintiff’s position is that this was a matter of affirmative defense, constituting an exception to the general risk insured against, which the garnishee was compelled to show in order to escape liability. Plaintiff rests upon the proposition that the duty of coming forward with evidence was the garnishee’s after plaintiff had made out what he contended was a prima facie case.

“When plaintiff proved that the liability had been incurred by defendant, in the form of a judgment entered against him, and that this was a liability explicitly insured against by appellant’s issuance of a policy then in force, he did make out a prima facie case which entitled him to have the issues submitted to the jury. That he made out his case largely through appellant’s admissions was immaterial. He was not required

in addition to show that none of the risks excepted in the policy, of which carrying passengers for hire was only one, were present when the accident occurred. When a defendant seeks to avail himself of a substantive defense reserved in a policy of insurance, when he relies upon a fact specifically mentioned in a policy as relieving him of a liability generally assumed in the policy, the defense becomes an affirmative one and the defendant at that point must shoulder the duty of coming forward with evidence in support of what he affirms. See *Bowers v. Great Eastern Casualty Co.*, 260 Pa. 147, 103 A. 536; *Watkins v. Prudential Ins. Co.*, 314 Pa. 497 at 508, 173 A. 644, 95 A. L. R. 869; and *Home Benefit Ass'n v. Sargent*, 142 U. S. 691, 12 S. Ct. 332, 35 L. Ed. 1160. * * * If the burden was on plaintiff in the present case to negative the risk excepted in the policy, 'it would necessarily follow that, for the same reason, he was required to establish the nonexistence of all the other stringent provisions by which the policy might be avoided,' as this court said in *Fisher v. Fidelity Mutual Life Ass'n*, 188 Pa. 1, 13, 41 A. 467, 468." (188 A. 125-126.)

In that case as in this the defendant attempted to draw an analogy between a policy similar to the one in the instant case and fire insurance and accident policies, claiming that in both the latter it is necessary for the plaintiff in one to prove that the loss was caused by fire and in the other by accident. In distinguishing between those cases and an indemnity case, the court stated:

"Appellant places its chief reliance on cases applying the well-established rule that in a suit

on a policy insuring against death by 'external, violent and accidental' means, the beneficiary, to make out a prima facie case, must prove not only death but the fact that it was caused by violence or accident, citing *Watkins v. Prudential Ins. Ass'n*, supra, and *Walters v. Western & Southern Life Ins. Co.*, 318 Pa. 382, 178 A. 499. In these cases the express condition of liability was not proof of death alone, but proof of death by accident. Accidental death is in such cases an operative fact and on plaintiff there always rests the duty of proving all such facts in order to recover on a contract." (188 A. 126.)

Again in *Center Garage Co. v. Columbia Ins. Co.*, 96 N. J. L. 456, 115 A. 401, the Court of Errors and Appeals of New Jersey stated:

"Clauses contained in policies of insurance which provide that the policy shall be void or the insurer relieved of liability on the happening of some event or the doing of or omission to do some act are not in any sense conditions precedent. If they are conditions at all, they are conditions subsequent, and constitute matters of defense, which, together with their breach, must be pleaded by the insurer to be available as a means of defeating a recovery on the policy; and the burden of establishing the defense, if controverted, is, of course, upon the party pleading it. *Joyce on Insurance*, vol. 4, par. 2190, and cases cited." (115 A. 402.)

In *The Law of Insurance—Joyce*, 2d Edition, Volume 5, pages 6221-2, the following appears:

"§ 3796a. *Excepted risks: burden of proof: evidence as to.*—If a risk is excepted by the terms

of a policy which insures against other perils or hazards such exemption from liability constitutes a defense which the insurer may urge, for it has not assumed that particular risk or risks and the burden rests upon insurer if it intends to take advantage of such exemption, so that it must allege and prove that the loss or a part thereof fell within the same.”

In *Arbuckle v. Lumbermens Mut. Casualty Co. of Illinois*, 129 F. (2d) 791, 793 (C. C. A. 2d 1942), the court stated:

“Although the plaintiff had the burden of proving the policy and that it covered Newman’s automobile the judge correctly charged that the burden of proving a breach of the condition that the car would be kept and used principally in Calicoon or vicinity was upon the defendant.”

The foregoing establishes the general rule applicable to the question. However, this case having arisen in California, and being in the Federal Court solely because of diversity of citizenship, in applying the law the Federal Court is in effect a State Court:

“For purposes of diversity jurisdiction a federal court is ‘in effect, only another court of the State’.”

Angel v. Bullington, 300 U. S. 183, 67 S. Ct. 657, 91 L. Ed. 832.

Furthermore, the laws of California govern a Federal Court’s construction of the policy (*Ocean Accident & Guarantee Corp. v. Torres*, 91 F. (2d) 464, 467 (9th C.C.A. 1937)).

With this in mind we now direct attention to the decisions of the California courts. In 14 *Cal. Jur.* at page 618, the general rule is thus stated:

“When the plaintiff has established a *prima facie* case, and the insurer claims exemption by reason of a breach of a proviso or condition subsequent, the burden rests upon it to prove that a loss, or a part thereof, falls within one of the prohibitive clauses of the policy, or, in other words, to prove the exception or breach relied on as defeating the plaintiff’s *prima facie* case.”

In *Dennis v. Union Mut. Life Ins. Co.*, 84 Cal. 570 (24 P. 120), one of the cases cited in support of the above text, it is stated:

“Thus one seeking to recover on an insurance policy must aver the loss and show that it occurred by reason of a peril insured against, but he need not aver the performance of conditions subsequent, nor negative prohibited acts, nor deny that the loss occurred from the excepted risks. (*Blasingame v. Home Ins. Co.*, 75 Cal. 635.) *Therefore the burden of proof was not upon the plaintiff to show what it was unnecessary to allege in his pleadings, and the court was right in its rulings.*” (Page 572.) (Italics added.)

See also:

Rossini v. St. Paul Fire etc. Ins. Co., 182 Cal. 415, 420 (188 P. 564);

Mah See v. North American Acc. Ins. Co., 190 Cal. 421, 425 (213 P. 42);

Bebbington v. Cal. Western etc. Ins. Co., 30 Cal. (2d) 157 (180 P. 673);

Bennett v. Northwestern Nat. Ins. Co., 84 Cal. App. 130, 137 (257 P. 586) ;

Mattson v. Maryland Casualty Co., 100 Cal. App. 96 (279 P. 1045).

In the case last cited the court at page 98 stated the rule as follows:

“It was sufficient for the plaintiff to prove the loss and that it occurred by reason of the peril insured against, and the burden of showing that the loss was produced through some excepted cause was upon the defendant (citing cases). The testimony in support of the allegations of the complaint was sufficient *prima facie* to have that result; and where this is true a motion for a nonsuit should be denied.”

Cardoza v. West American Com. Ins. Co., 6 Cal. App. (2d) 500 (44 P. (2d) 668), was an action against the defendant insurance company to recover on an automobile indemnity policy. One of its defenses was that at the time of the accident the operator was conveying a passenger for consideration, which under the terms of the policy relieved it from liability. In considering this question the court reiterated the rule:

“The burden was on the defendant to prove its allegation that the policy was rendered void for the reason that the car was being used at the time of the accident to convey a passenger for hire.” (Page 502.)

**PLAINTIFFS' PRIMA FACIE CASE WAS NOT OVERCOME BY
THE TESTIMONY OF DEFENDANT'S WITNESS AS A MAT-
TER OF LAW.**

In his opinion the trial judge further states:

“Liability does not attach unless the truck, whether alone or with the trailer attached, was actually being used in the transportation of merchandise for hire. And when the facts are not disputed—whether the truck was, at the time of the accident, engaged in the sole activity covered by the policy is a question of law for the court.”
(T. 58.)

This is couched on the theory that the undisputed evidence establishes that the truck was not *actually* being used in the transportation of merchandise. In order to so conclude, it would be necessary to usurp the function of the jury and (1) base this conclusion on selected parts of the testimony of Warner, a discredited witness called by defendant, and (2) disregard that portion of the testimony of Warner indicating that the use being made of the tractor at the time of the accident was incidental to the operation of his business of transporting merchandise.

That the witness, Warner, was discredited is fully shown in the opinion, wherein the trial judge in referring to his testimony states:

“His story is contradictory. The version he gave on the first day of the trial as to the object of his trip from San Francisco differs from that which he told at the trial in the Superior Court, and at a hearing in this court in an action for declaratory judgment, to which he was made a party,

and in which a declaration of non-coverage was secured against him and his co-partner. * * *"

(T. 55.)

"We are confronted here with the inherent improbability of a story, which bears almost on the fantastic."

(T. 57.)

Regardless of the opinion entertained by the trial judge as to the credibility of the witness, it was the prerogative of the jury to pass on his credibility. Thus, in the case of *Wendorff v. Missouri State L. Ins. Co.*, 318 Mo. 363, 1 S.W. (2d) 99, 57 A.L.R. 615, the Court stated:

"The defense thus tendered was an affirmative defense, and, as appellant says, the burden was on respondent to establish it. (citing) It is furthermore the general rule in such circumstances that the plaintiff's case cannot be taken from the jury, for he has the right to have the jury pass on the credibility of the defendant's witnesses and the weight of their testimony, though uncontroverted. (citing) But the rule has its exceptions. When the proof is documentary, or the defendant relies on the plaintiff's own evidential showing (or evidence which the plaintiff admits to be true), and the reasonable inferences therefrom all point one way, there is no issue of fact to be submitted to the jury." (57 A. L. R. 618-19.)

The same result was obtained in *Anthony v. Mercantile Mutual Accident Association*, 162 Mass. 354, 38 N. E. 973, 26 L. R. A. 406, wherein the Massachusetts Supreme Judicial Court stated:

“The burden being on the defendant to prove that it was from one of the excepted causes, the question remains whether the jury should have been instructed as a matter of law that the burden was sustained. It is not often, where a party has the burden of proving a fact by the testimony of witnesses, that the jury can be required by the court to say that the fact is proved. They may disbelieve the witnesses. If the conclusion is to be reached by drawing inferences of fact from other facts agreed, ordinarily the jury alone can draw these inferences. It is only when no inferences are possible except those which lead to one conclusion that the jury can be required to find a proposition affirmatively established.” (26 L.R.A. 407.)

It is difficult to conceive, and we have found no cases holding, that a directed verdict can be granted upon evidence offered by a defendant after a plaintiff has once established a *prima facie* case. In *Peterson v. Chicago & A. Ry. Co.*, 265 Mo. 462, 178 S.W. 182, 187, the Court in discussing this question stated:

“As held in paragraph 1 of this opinion that, the plaintiff having made out a *prima facie* case, then according to the rule just announced the burden rested upon the defendant to disprove and overcome that case, to the satisfaction of the jury. That, of course, means that the jury and not the court must pass upon the credibility of the witnesses and the weight to be given their testimony. *That is, that after a prima facie case has once been made out, the case can never be taken from the jury.*” (Italics added.)

Again in the case of *Lederer v. Railway Terminal & Warehouse Co.*, 346 Ill. 140, 178 N. E. 394, 77 A.L.R. 1497, the Illinois Supreme Court stated:

“If the evidence in support of the plaintiff’s allegations is sufficient to make a prima facie case, the trial court is not authorized to direct a verdict for the defendant because of evidence of contrary facts tending to an opposite conclusion.” (77 A.L.R. 1500.)

The defendant in the court below and the trial judge in his opinion place considerable emphasis on cases that uphold the defense of insurance companies where the vehicle at the time of the accident is being used for a purpose contrary to the terms of the policy (T. 62, 63). Principal among these cases is *Foster v. Commercial Standard Insurance Company*, 121 F. (2d) 117 (C.C.A. 10th, 1941). We take no issue with the rule enunciated in that case and the others cited, as we have never contended and do not now contend that where such defense is established an insurance company cannot be relieved of liability. The significant thing, however, is that *in all of these cases the nonconforming use of the vehicle was either expressly admitted by the claimant or not made an issue*. This fact clearly appears in that portion of the *Foster* case that is quoted in the opinion. “‘The damage *admittedly* was incurred while the insured was operating the truck for pleasure and outside the coverage of the policy?’ ” (T. 63—italics added.) Obviously, under such circumstances there can be no question concerning this fact to be submitted to the jury, and it is purely one of law upon which the Court can act.

In *Blank v. Coffin*, 20 Cal. (2d) 457 (126 P. (2d) 868), the Supreme Court of California enunciated the rule that is here applicable and we believe determinative of this question.

“Usually, the opposing party introduces evidence as to the nonexistence of the fact in issue, and the jury must then determine the existence or nonexistence of the fact from all the evidence before it. If the evidence contrary to the existence of the fact is clear, positive, uncontradicted, and of such a nature that it can not rationally be disbelieved, the court must instruct the jury that the nonexistence of the fact has been established as a matter of law. (citing) The jury, however, is the sole judge of the credibility of the witnesses (Cal. Code Civ. Proc., sec. 1847; see cases cited in 27 Cal. Jur. 182, sec. 156) and is free to disbelieve them even though they are uncontradicted if there is any rational ground for doing so. (citing.) In most cases, therefore, the jury is free to disbelieve the evidence as to the nonexistence of the fact and to find that it does not exist on the basis of the inference.” (20 Cal. (2d) 461.)

In the recent case of *Nash v. Wright*, 82 Cal. App. (2d) 467 (186 P. (2d) 686), the court set out four rules applicable to the question here involved:

“Such demonstration will be facilitated by keeping in mind four cardinal rules which are inalienable from a fair consideration of a judgment based upon a directed verdict: (1) On a motion for such verdict the same conditions as to the proof must obtain as on a motion for nonsuit. (2) Upon such motion it is the trial court’s duty to give plaintiff’s evidence all the value to which

it is entitled, and ignoring conflicts in the testimony, to indulge every legitimate inference reasonably deducible from the proof in favor of plaintiff. (*Mairo v. Yellow Cab Co.*, 208 Cal. 350, 351 (281 P. 66); *Dieterle v. Yellow Cab Company*, 34 Cal. App. (2d) 97, 98 (93 P. (2d) 171).) (3) Under such motion, *the evidence for the defense must be disregarded*, and if there is any substantial evidence from which the jury can find for plaintiff it is the court's duty to deny the motion. (4) *On appeal from a judgment after directed verdict the reviewing court cannot affirm the judgment if the evidence of plaintiff standing alone would have warranted findings favorable to him* (*Anthony v. Hobbie*, 25 Cal. (2d) 814, 817 (155 P. (2d) 826)), *and only the evidence most favorable to the plaintiff may be examined.*" (Page 470.) (Italics added.)

In considering the probative effect of inferences as against direct evidence introduced by a defendant who moves for an instructed verdict, the court further stated: "But on a motion for an instructed verdict such rule does not authorize the dispelling of inferences by evidence introduced by the defendant." (Page 472.)

In *Lindemann v. San Joaquin Cotton Oil Co.*, 5 Cal. (2d) 480 (55 P. (2d) 870), the Supreme Court of California at pages 503-4 enunciated the same rule:

"Subject to the exercise of legal discretion, the jury is the sole judge of the weight, effect and sufficiency of the evidence to establish any fact for which it may be offered. The jury is the sole judge of the credibility of the witnesses and *may*

believe all of the testimony of a witness or believe a part and reject parts as it may be convinced of the truth or falsity of such testimony, whether it arises from wilfulness or mistake" (Italics added).

In *Burgess v. Cahill*, 26 Cal. (2d) 320 (158 P. (2d) 393), the same court stated the oft-repeated rule:

"The settled rule is that a court may direct a verdict only when, disregarding conflicting evidence and giving plaintiffs' evidence all the value to which it is legally entitled, indulging in every legitimate inference which may be drawn therefrom, the result is a determination that there is no evidence of sufficient substantiality to support a verdict in favor of the plaintiffs" (pages 321-2).

The Federal Courts have adhered to these general principles. (*Berry v. United States*, 312 U.S. 450, 61 S. Ct. 637, 85 L. Ed. 945; *Montgomery Ward & Co. v. Duncan*, 311 U.S. 243, 61 S. Ct. 189, 85 L. Ed. 147; *Aetna Casualty & Surety Co. v. Yeatts*, 122 F. (2d) 350 (C.C.A. 4th); *Banks v. Associated Indemnity Corporation*, 161 F. (2d) 305 (C.A.A. 5th 1947); *Simmonds v. Capital Transit Co.*, 147 F. (2d) 570, U.S.C.A., D.C. 1945; *Terminal Railroad Ass'n v. Staengel*, 122 F. (2d) 271 (C.C.A. 8th 1941).)

In *Simmonds v. Capital Transit Co.*, supra, as in the instant case, judgment was granted for defendant notwithstanding the jury's verdict in favor of plaintiff. In reversing the judgment the court stated:

"It requires us, in deciding whether to uphold the verdict of the jury or the judgment of

the Court to balance the weight of the evidence against the judge's determination and in favor of the jury's determination; the question being, not whether there is sufficient evidence in the record to support the judge's findings and decision, but whether there is sufficient evidence, when construed most favorably for the party upon whom the onus of proof is imposed, from which a jury of reasonable men could properly have reached the verdict which was reached. * * *

"It is true that there was conflicting and contradictory evidence and the trial judge was justified in concluding that the evidence preponderated against appellant's allegations and contentions. But that was not the test to be applied upon a motion n. o. v. * * * In other words, construing the evidence most favorably to appellant and giving him full effect of every legitimate inference therefrom—as the law requires—reasonable men might well differ in their conclusions, upon the evidence so considered. No more is required to sustain the verdict against a motion for judgment n. o. v." (Page 571.)

THE JURY HAD THE RIGHT TO CONCLUDE THAT THE VEHICLE WAS BEING USED FOR TRANSPORTATION OF MERCHANDISE PURPOSES.

If we are correct in our conclusion that plaintiffs established a prima facie case, and that the defendant had the burden of proving the affirmative allegations of its answer, and that the jury had the right to disregard all or any part of the testimony of defendant's

witness relating to this defense, our discussion under this title is surplusage.

Assuming without conceding that it is necessary to consider any of the testimony of Warner, it cannot be disputed that where, as here, the case was taken from the jury, it is the duty of the Court to only consider that testimony that is favorable to our position, and indulge in every legitimate inference which may be drawn therefrom.

(*Burgess v. Cahill*, *supra*, 26 Cal. (2d) 320 (158 P. (2d) 393).

The opinion of the trial Court states: "Liability does not attach unless the truck, whether alone or with the trailer attached, was actually being used in the transportation of merchandise for hire" (T. 58). This conclusion is not sustained by the provision of the policy relied upon by the defendant. Without at this point discussing the effect of the Railroad Commission endorsement, we again call attention to this provision.

"The automobiles described are and will be used only for transportation of merchandise *purposes* and will be operated as follows, and this insurance covers for no other use or operation." (T. 11). (*Italics added.*)

The words "will be operated as follows" indicate that some description of the mode of operation of the automobiles is thereafter stated in the policy, but on the contrary it is conspicuous by its absence. Hence, we have for consideration the language "will be used only for transportation of merchandise purposes". We have emphasized the word "purposes", as we

take the position that the fair import to be accorded this provision is that the vehicle only need be used for such purposes, which does not mean that it must at all times be physically transporting merchandise.

“The word ‘purpose’ means ‘that which a person sets before himself as an object to be reached or accomplished; the end or aim to which the view is directed in any plan, manner or execution’.”

In re McCoy, 10 Cal. App. 116, 129 (101 P. 419).

The testimony of Warner discloses sufficient facts to justify the jury in concluding that at the time of the accident he was using the tractor for transportation of merchandise purposes. On this point attention need only be directed to the fact that he had no definite route, he wildecatted (T. 103). At the time of the accident he was returning after having delivered a cargo, for compensation (T. 106), and he was taking the most direct route back to his point of origin (T. 126). In addition to returning to pay his insurance premium, one of his purposes in returning was to discuss with one Dowdell the hauling of a load (T. 127).

Regardless of what his intent was, the fact remains that at the time of the accident he was returning to his point of origin, even if it be conceded that he had the additional intent to again return to Blue Lakes for his trailer. The liability under a policy of insurance is determined by the use of the vehicle at the time of the accident and not by the intention of the

driver. (*Nichols v. Hawkeye Casualty Co.*, 233 Ia. 792, 10 N.W. (2d) 533).

In his opinion the learned trial judge cites a number of cases in which insurance companies were held liable for uses of the vehicle that were incidental to that permitted by the terms of the policy, and on this subject states:

“Behind all these cases runs the norm that if the vehicle, at the time of the accident, can be said to be on a mission incident to the object to which its use is limited, the courts will give full effect to the policy.” (T. 59.)

Thus, the opinion and the cases cited therein indicate that on a “return trip” after delivering a cargo for compensation the insurance covers even though at the time of the accident there was no merchandise being transported. Commencing with this premise, which of the two trips from Blue Lakes to San Francisco was the return trip? Pausing here to indulge in an assumption for the purpose of illustration, assume that the first return had been uneventful, and the accident occurred on the second return to San Francisco. Under such circumstances, could not the defendant with at least equal plausibility claim that this second trip was not incidental to the permitted use of the tractor, as Warner had previously returned to his point of origin after delivering his cargo?

In any event, can there be any doubt that the question is not one of law for the court to decide, but one for the jury after considering all the facts and

circumstances and drawing all proper inferences therefrom?

If liability attached under the policy, it did so at the time of the accident, and was not affected by the fact that Warner intended to or did in another trip subsequently return for his trailer. Further illustrating the fallacy of the reasoning that forms the basis of the judgment from which we are appealing, assume that Warner had ultimately decided to abandon the trailer, or that he had arranged with someone else for its delivery to San Francisco. Does the liability of the defendant turn on his secret intent or on his overt acts as found by the jury? It is noteworthy that according to his testimony, he often used the tractor alone for the transportation of merchandise (T. 141), and for hauling loaded trailers belonging to others. (T. 138-139.) Moreover, it is significant that the policy insures the tractor and trailer as separate units, and not necessarily in combination with each other. (T. 25, 34.)

In *Ocean Accident & Guarantee Corp. v. Torres*, 91 F. (2d) 464 (C.C.A. 9th 1937), the interpretation there applied is analagous to that which we advocate here. There the appellant contended that the place of the accident and the nature of the service the appellee was performing at the time of the accident refuted the contention that she was performing household domestic service. In disposing of this contention, this Court stated:

“The appellant, however, argues that: ‘Both the place of the accident and the nature of the

service Miss Torres was performing at the time of accident refute a contention that she was performing "household domestic service". It is pointed out that the place of the accident was four or five miles from the 'household' of the Brinkmans, and it is contended that the nature of the service 'pertained more to trucking or parcel delivery and was not even remotely translatable into "household domestic service".'

"We do not concur, however, in the appellant's assumption that household service must necessarily be performed on the premises occupied by the household. It is the *nature* of the task, and not the *place of performance*, that determines its character. The appellee was returning some tubs that she had used in doing laundry work for her employer, Mrs. Brinkman. In other words, she was doing work incidental to the completion of a household chore." (Page 470.)

In *Journal Co. v. General Acc. Fire & Life Assur. Corp.*, 188 Wis. 140, 205 N.W. 800, the policy there involved restricted the use of the vehicle to the transportation of materials or merchandise. After making a delivery, the accident occurred on a return trip, although there were still a couple of packages left in the truck. In upholding the recovery, the court held that the policy not providing that the transportation of materials or merchandise being the dominant purpose of the use of the vehicle, an incidental use was sufficient to hold the insurer.

Again in *Mitchell v. Great Eastern Stages*, 140 Ohio St. 137; 42 N.E. (2d) 771, 773-4:

“So the purpose in requiring such a policy is, in the last analysis, the protection of the traveling public. To attain this purpose the policy must be given a liberal and broad interpretation in favor of the insured and those claiming under and through the insured * * *.

“Busses operating in the common carriage of passengers must be serviced and repaired and, when not in use, must be housed; so for these purposes they must be taken to service stations, repair shops or garages. Moreover, in accomplishing these ends it is often necessary to leave routes specified in the certificate of public convenience and necessity granted by the commission. Such movements of a bus, not engaged in carriage at that time, would not be limited to specified routes for those might not lead to the proper destination; nor can it be said that a certificated common carrier has ceased to operate as such in doing things incidental to the repairing, servicing and housing of its busses. It would be a very narrow construction to hold that such operation ceased when it became necessary to unload passengers and drive around the square to a garage for repairs. In doing reasonably necessary traveling upon highways to accomplish these incidental things the common carrier is as much engaged in the business of common carriage as when actually transporting passengers upon specified routes. See *Rusch v. Mielke*, 234 Wis. 380, 291 N.W. 300; *Liberty Mut. Ins. Co. v. McDonald*, 6 Cir., 97 F. (2d) 497.”

In *Smith v. California Highway Indem. Exch.*, 218 Cal. 325 (23 P. (2d) 274), the plaintiffs brought

an action against the insurance carrier to recover a judgment obtained against its insured. The policy provided that the vehicle was to be operated as a jitney bus, and shall not cover any acts that may occur while it is being operated for any other purpose. The accident occurred when the insured was leaving his home and while he was not on the route over which he was authorized to conduct the jitney bus. In upholding a recovery by plaintiff, the court stated:

“It cannot be doubted that the Chandler automobile was ‘maintained’ by Davis for the purpose and business of a jitney bus at the time of the accident. It was operated at the time ‘in the service of the subscriber as a jitney bus * * * within the city and county limits of the city of San Francisco’, and it may not fairly be said that the car was at the time operated for any other purpose than that of a jitney bus. Necessarily Davis was required to keep the car somewhere and it was kept at his home which was the place specified in his operator’s permit where it was to be kept and which was in the vicinity of the Twenty-ninth and Mission terminus of the route. At the time of the accident he was operating, using and maintaining his car with the equipment, plates and badge placed and displayed as required by local regulations. The policy did not specify the particular or any route over which the car should be operated. The limits of the operation thereof were the city and county of San Francisco. We have no hesitancy in concluding that the accident was included within the terms of the policy considered as an independent document.” (Pages 327-28.)

The legal effect of the endorsement required by the Railroad Commission that is attached to the policy (T. 89) makes the company liable to the plaintiffs for the damages sustained in this accident whether the vehicle was or was not transporting merchandise, unless the exception numbered 4 therein is applicable.

“(4) any loss arising out of any operations of the insured except operations authorized or for which authorization is required under the afore-said statutes”.

In other words, if returning to the point of origin after delivering merchandise for compensation with the intent of soliciting and hauling for Dowdell *is an operation authorized or for which authorization is required under the statutes*, the endorsement in itself overcomes the effect of the declaration in the policy upon which defendant relies.

The legal effect of similar endorsements has been discussed in *Travelers Mut. Casualty Co. v. Thornsbury*, 276 Ky. 762, 125 S.W. (2d) 229; *Central Mut. Ins. Co. v. Tartar*, 92 F. (2d) 829, (C.C.A. 6th), and in *Liberty Mut. Ins. Co. v. McDonald*, 97 F. (2d) 497, (C.C.A. 6th). In the case last cited the Court states:

“Appellant further contends that at the time of the collision 'Tractor No. 18 and trailer were not being 'operated' in the sense of the statute, since after they had broken down the cargo was removed, and they were simply standing empty on the highway. Without deciding just when the operation of the equipment terminated, it is clear enough that it had not ceased while the unit was

still parked on the highway as a result of disablement.”

The language used in the endorsement must be interpreted in the light of its purpose and liberally in favor of the insured.

“Then again, in construing a writing, all parts are to be considered with reference to each other, and in the case of a contract of insurance, the contract is to be interpreted in the light of its nature in view of its purpose as such, and with a considerable degree of liberality in favor of the insured and against the insurer by reason of it having framed the contract. A risk fairly within contemplation is not to be avoided by any nice distinction or artificial refinement in the use of words.”

Granger v. New Jersey Ins. Co., 108 Cal. App. 290, 293 (291 P. 698).

CONCLUSION.

The conclusions of the trial judge and many of the authorities cited by him would be applicable if the order here involved, from which this appeal is taken, had been upon a motion for a new trial. On the hearing of such motion the discretion of a trial judge, and the powers he may exercise, are almost as plenary as they are limited on a motion for directed verdict, or for judgment notwithstanding a verdict, which is here involved.

In view of the fact that he does not directly discuss the difference in his function between acting upon the

order here granted and the motion for a new trial, which he denied, we feel that he was led into error by confusing his prerogative of weighing the evidence on a motion for a new trial with the limited function that he is required to perform on a motion for directed verdict. Notwithstanding that the record and the facts establish the contrary, it is apparent that the trial judge did not intentionally usurp the function of the jury, as in this connection his opinion states:

“This conclusion still calls for the disposition of the motion for a new trial.

“I realize that this motion could be granted condition on its taking effect only if the judgment notwithstanding the verdict is reversed on appeal.

“However, in this case, the motion for a new trial should be denied. Obviously, if my interpretation of the insurance policy is correct, the jury’s verdict is wrong.

“If the jury’s verdict is right, it can only be because the case presented a factual situation for their solution.

“If this be so, then—despite what is said in this opinion about the unsatisfactory character of the testimony concerning the nature of the trip on which the accident occurred—I should allow the jury’s conclusion upon the facts to stand and not substitute my own for it.

“The motion for a new trial will, therefore be denied.” (T. 65-66.)

Following the trial of this cause all of the questions of fact were duly submitted to the jury upon proper instructions of the court, after which the jury unani-

nously brought in a verdict in favor of the plaintiffs for the amounts prayed for in the complaint. The action of the trial court in entering judgment for defendant notwithstanding the verdict in favor of the plaintiffs was erroneous, and said order and the judgment based thereon should be reversed.

Dated, Berkeley, California,
January 7, 1949.

Respectfully submitted,
NATHAN G. GRAY,
Attorney for Appellants.

No. 12,056

IN THE

United States Court of Appeals
For the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA
L. BOULTER,

Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Appellee.

Appeal from the United States District Court for the
Northern District of California, Southern Division.

BRIEF FOR APPELLEE.

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No. 12,056

IN THE

**United States Court of Appeals
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GEORGE W. BOULTER and MARGRETTA
L. BOULTER,

Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Appellee.

Appeal from the United States District Court for the
Northern District of California, Southern Division.

BRIEF FOR APPELLEE.

FOREWORD.

Plaintiffs and appellants argue (i) that they establish a *prima facie* case (App. Op. Br. pp. 14-15), (ii) that defendant and appellee had the burden of proving the tractor "*was not being used*" for transportation of merchandise purposes (App. Op. Br. pp. 15-22), (iii) that their (claimed) *prima facie* case was not overcome by the testimony of defendant's witness as a matter of law (App. Op. Br. pp. 23-30), and (iv) that the jury had the right to conclude that the vehicle was being used for transportation of merchandise purposes (App. Op. Br. pp. 30-39). We

shall answer these arguments in the order indicated in the subject index, although we respectfully submit that the opinion* of Judge Yankwich (Tr. 53-74) very ably covers all the points raised by the appellants and demonstrates that they are without merit.

In this brief, italics are our own, except as to those appearing in passages taken from Judge Yankwich's opinion, in which instances they are used in lieu of the underlining which Judge Yankwich used.

ARGUMENT.

I.

THERE IS NO MERIT IN PLAINTIFFS' (APPELLANTS') CLAIM THAT DEFENDANT (APPELLEE) HAD THE BURDEN OF PROVING THAT THE TRACTOR WAS NOT BEING USED FOR TRANSPORTATION OF MERCHANDISE PURPOSES; ON THE CONTRARY, AS USE OF THE VEHICLE FOR TRANSPORTATION OF MERCHANDISE PURPOSES WAS THE ONLY USE COVERED BY THE POLICY IN QUESTION, PLAINTIFFS HAD THE BURDEN OF PROVING THAT, AT THE TIME AND PLACE OF THE ACCIDENT IN QUESTION, THE VEHICLE WAS BEING USED FOR SUCH PURPOSES.

Appellants have argued at length that "the defendant had the burden of proving that the tractor was not being used for transportation of merchandise purposes" (App. Op. Br. pp. 15-22).

Appellants assert that Appellee does not question "the sufficiency of the admissions and evidence to establish" the allegations of the complaint (App. Op. Br. p. 15), and then go on to affirm that "the only

*The opinion is reported in 78 Fed. Supp. 895.

question remaining on this subject is whether it was incumbent upon plaintiffs to have gone further and negated the affirmative defenses pleaded in the answer," (App. Op. Br. p. 15).

It is clear, we submit, that Appellants have misconceived the entire nature of the cause of action which they are seeking to establish, and that their misconception is based upon a disregard of the nature and plain terms of the policy on which they seek to recover.

Appellants allege in paragraph IV of their complaint (Tr. p. 4) that the defendant (Appellee) issued a liability policy under which it undertook to pay any sums its assured was required to pay on any claims "*caused by accident and arising out of the ownership, maintenance, or use of a certain 1939 Dodge Tractor * * **" (Tr. p. 4.)

This allegation is denied in paragraph III of defendant's answer (Tr. p. 10).

It is obvious that it was incumbent on plaintiffs to prove the existence of the insurance policy referred to in their complaint. Plaintiffs, as a part of their case in chief, introduced the policy in evidence (Plaintiffs' Exhibit No. 1, Tr. pp. 25-42; pp. 88-92).

The policy on which plaintiffs seek to recover is not a policy covering all uses of the vehicle therein described. It is a policy which covers the vehicles therein described while they are "used only for transportation of merchandise purposes" (Tr. p. 25).

The distinction is well stated in Judge Yankwich's opinion (Tr. 61):

“The defendant did not insure against all the risks of the plaintiffs while engaged in the business of trucking, but only against a specific risk. Otherwise put, it insured the automobiles when ‘*used only for transportation of merchandise purposes.*’ ”

That it is incumbent upon *plaintiffs* to prove, when seeking to recover on a policy of this type, that the vehicle in question was, at the time of the accident, being used for *the only purposes covered by the policy*, and that the burden of such proof is on the plaintiffs, is established beyond controversy (we submit) by the numerous authorities which have dealt with the subject.

The general rule is stated as follows in 21 “Insurance Law and Practice”, by Appleman. Section 12272, page 126, where the commentator makes the following observation:

“The plaintiff must prove that an automobile causing the injury was one of the automobiles operated in the insured's business, insured under a blanket liability policy. The plaintiff may also be required to prove that the vehicle was operated in the business or service authorized by a certificate or permit. It is also necessary to prove that the truck was operated for commercial purposes, where that is the sole coverage of the policy.”

The leading case upon the subject appears to be *Habedank, et al. v. Atlantic etc. Insurance Co.* (1942), 128 N.J.L. 338, 25 Atl. (2d) 889. In that case the Appellate Court sustained a judgment of nonsuit in an action by which the plaintiff sought to compel an insurance carrier to pay a judgment against its assured. The Court stated:

“One of the warranties contained in the policy provided that the automobile would be used only for ‘commercial’ use and the policy further specifically provided that it was not to cover any liability of the assured arising out of the use of the automobile for any purpose other than that just specified. The learned trial judge ruled that appellants failed to prove that the automobile was used for a commercial use and * * * granted a non-suit. Judgment was entered accordingly. The propriety of that judgment is challenged. * * * Under the particular policy of insurance before us * * * we think that as a condition precedent to recovery, it was incumbent upon appellants to prove not only permission, but also that the automobile, at the time of the accident was operated for a ‘commercial use’ as specified in the policy. * * * It was not a condition subsequent * * * Here the condition in the policy was that the car be used for ‘commercial use’ is in the nature of a ‘promissory warranty’, a ‘condition precedent’ to the right of recovery * * * It is a condition which has been likened to an ‘exception’ or ‘proviso’ in the enacting clause of a statute. Under such circumstances, the pleadings and proof must show the facts to be outside the ‘exception’ or ‘proviso’ and within the general

clause, but if the 'exception' or 'proviso' be elsewhere than in the enacting clause that is something to be set up in an answer or plea."

Numerous authorities are in accord.

In *Jones v. Manufacturers Cas. Ins. Co.* (1942), 313 Ill. App. 386, 40 N. E. (2d) 545, the Court said:

"The burden of proof rests upon the plaintiffs to establish that the use made by the assured of the truck at the time of the collision came within the coverage of the policy." (40 N. E. (2d) 547.)

In *Lavine v. Ind. Ins. Co. of N. A.* (1933), 260 N. Y. 399, 183 N. E. 897, the liability policy upon which the plaintiff sought recovery provided coverage for use of a vehicle in connection with the assured's place of business in Albany, New York. The Court stated:

"As a conclusion of law, the trial court found that the insurance company, having pleaded that the Studebaker automobile was not being used when the accident occurred in connection with assured's Albany place of business, and that the loss was not within the coverage of the policy, the burden of proof thereof was upon the defendant, and further that the defendant failed in its burden of proving said defense. In those conclusions we think the trial court was in error." (183 N. E. 899.)

* * * * *

"The burden of proof rested upon the plaintiff to establish that the policy covered. That burden was not shifted to the defendant, because of an affirmative allegation in the answer to the effect that the policy did not insure against the accident

in question. The denials in the answer raised an issue as to whether the accident came within the indemnity coverage provided in the policy. That was the issue, and not whether liability did not exist under the policy because the accident fell under some provisions of the policy relieving the defendant from liability.” (183 N. E. 900.)

Attention is directed to the portion of the opinion last quoted in which the Court points out that the “burden was not shifted to the defendant, because of an affirmative allegation in the answer to the effect that the policy did not insure against the accident in question”.

Defendant in the instant case, in addition to denying the general allegation of coverage (Tr. p. 10), pleaded that the vehicle at the time of the accident was not being used for transportation of merchandise purposes (Tr. pp. 11-13). That this matter was so pleaded does not shift the burden of proof. The law on this point is clear and is well stated in the opinion just referred to, as well as in numerous other cases. See, for example, *Kellner v. Travelers Insurance Co.* (1919), 180 Cal. 326 at 330, 181 Pac. 61.

See, also:

Manthey v. Am. Auto Ins. Co. (1941), 127 Conn. 516, 18 Atl. (2d) 397:

“Where * * * the defendant raises the issue of violation of some particular condition of the policy by a special defense, the burden of proving this issue is on the plaintiff.” (18 Atl. (2d) 399.)

* * * * *

“The quotations from the policy show coverage as to commercial use * * * The plaintiff had the burden of proving that the coverage existed, and having failed to do so the judgment of the trial court was correct.” (18 Atl. (2d) 399.)

Liberty Mutual Ins. Co. v. Martel (1937), 88 N. H. 479, 192 Atl. 152:

Syll. para. 1:

“In suit by insurer to determine question of coverage under automobile liability policy, insurer did not have burden of proof on issue of non-coverage.”

Whitlock v. Individuals etc. Assn. (1932), 138 Ore. 383, 6 Pac. (2d) 1088:

Syll. para. 4:

“In action against insurer on blanket liability policy, it was necessary to prove that automobile causing injury was one of autos operated in insured’s business (Laws 1925, p. 756).”

Smith v. Rep. Underwriters (1940), 152 Kan. 305, 103 Pac. (2d) 858:

“Having given consideration to the commercial operations provided for in the certificate or permit—and therein specifically set out—the company issues a policy covering vehicles engaged in such operations. It does not insure vehicles otherwise engaged—that is, which are being used for commercial, personal or social purposes outside the operations covered by the permit * * * It was clearly part of the plaintiff’s case to show insurance coverage * * * If a private car covered by

the usual policy is involved in an accident, the plaintiff in an action against the insurance carrier must show that the policy covers the car therein described. A plaintiff has the same burden to show coverage when the issue of coverage turns, not upon description of the vehicle, but upon whether it was being used in operations authorized by the permit" (103 Pac. (2d) 860).

Numerous California cases dealing with insurance litigation are in line with the rule above referred to.

Thus in *Allen v. Home Insurance Co.* (1901), 133 Cal. 29, 65 Pac. 138, a fire policy covered a building "*while occupied as a dwelling house*"; the Court held that, as insurance extended *only for such use of the insured premises*, it was an essential part of the plaintiff's case that she plead and prove such use. The Court stated, in this respect:

"The allegation was not merely a condition precedent, as referred to in section 457 of the Code of Civil Procedure. It went to the very essence of plaintiff's right to recover. Certain conditions subsequent to the right of recovery, matters of defense, the non-performance of conditions subsequent, and certain negative prohibited acts need not be pleaded by plaintiff; but the rule does not extend to the essence of the cause of action" (133 Cal. 30).

A similar holding appears in *Arnold v. American Insurance Co.* (1906), 148 Cal. 660, 84 Pac. 182, where fire coverage was provided on a building "*while occupied as a dwelling house*". In an action on the policy,

the Court held that the failure of the plaintiff to allege such use rendered his complaint defective, and approved the holding of *Allen v. Home Insurance Co.*, *supra*.

In *Agalianos v. American Central Insurance Co.* (1923), 62 Cal. App. 349, 217 P. 107, a fire policy provided coverage on a building “*only while occupied for mercantile and restaurant purposes*”. The Court stated:

“It has been held that where, as here, the action is to recover on an insurance policy, a cause of action is not stated unless it be shown by the complaint that the loss alleged was within the terms of the policy. In this case, therefore, under the construction placed by the defendant upon the above provision of the contract between the insurer and the insured, it was, to state a cause of action against the defendant, indispensably necessary to allege that the building destroyed was, at the time of the fire, used by the insured for mercantile and restaurant purposes” (62 Cal. App. 353).

See also:

Balan v. National Union Fire Ins. Co. (1912),
19 Cal. App. 778, 127 P. 829,

where the Court held that the complaint did not state a cause of action where it “contained no statement showing that the buildings were being put to the particular uses limited by the insurance contract at the time they were destroyed” (19 Cal. App. 779).

The general rule is also stated in *Ells v. Order of United etc. Travelers* (1942), 20 Cal. (2d) 290, 125

Pac. (2d) 457, where a plaintiff was seeking to recover on a contract of insurance which insured against accidental death. The Court stated:

“The burden was on the respondents [plaintiffs] to establish as a part of their case that death resulted from an accident, as defined by the terms of the contract of insurance, and it was not incumbent on the appellant to prove that death was not caused by accident” (20 Cal. (2d) 304).

We are not unmindful of cases (such as those cited by Appellants in their opening brief, pages 15-22) in which courts have held that the burden is on an insurance company to prove facts which bring into operation *an exception to general coverage* or a condition subsequent. Those cases, however, are not pertinent in this case, because here the *only coverage* provided is coverage on a vehicle while “used only for transportation of merchandise purposes * * * and * * * for no other use or operation” (paragraph 5 of “Declarations”, Tr. p. 25).

Akin to the rule above referred to is the rule long adhered to that a plaintiff seeking to recover on a liability policy which extends coverage to cars used only with the permission of the assured must sustain the burden of proving permissive use.

Thus, in *Denny v. Royal Indemnity Company* (1927), 26 Ohio App. 566, 159 N. E. 107, the court on appeal affirmed a directed verdict in favor of defendant insurance carrier where it appeared that the record was “absolutely silent on the question of permission to use the car” (157 N. E. 109).

See also

Bowen v. Cote (C. C. A. 1, 1934) 69 Fed. (2d) 136.

It is respectfully submitted that the above authorities establish beyond controversy that in this case plaintiffs (appellants) had the burden of proving that the vehicle was engaged in an operation covered by the policy (i.e. that it was being used for "transportation of merchandise purposes") at the time of the accident and that defendant (appellee) was required to assume no burden of proof on this issue.

II.

THERE IS NO MERIT IN PLAINTIFFS' (APPELLANTS') CLAIM THAT THEY "ESTABLISHED A PRIMA FACIE CASE"; ON THE CONTRARY, IN VIEW OF PLAINTIFFS' FAILURE TO SHOW AFFIRMATIVELY AS PART OF THEIR CASE IN CHIEF THAT THE VEHICLE WAS ENGAGED IN ANY USE COVERED BY THE POLICY, THE PLAINTIFFS WHOLLY FAILED TO ESTABLISH A PRIMA FACIE CASE.

Appellants argue (App. Op. Br. pp. 14-15) that they established a *prima facie* case.

It is hardly necessary to point out that in order for plaintiffs to establish a *prima facie* case, it was incumbent upon them to show facts which would entitle them to recover on the policy which is the subject matter of this action. Their failure, after placing the policy in evidence, to show that at the time of the accident the vehicle described in the policy was being used for any use covered by the policy rendered their case in chief fatally defective.

The authorities cited under point I (*supra*) establish this proposition. See, particularly, *Habedank, et al v. Atlantic etc. Insurance Company* (*supra*), p. 5, in which the Appellate Court sustained a judgment of non-suit granted when plaintiff failed to show an insured use. And see *Mawhinney v. Southern Insurance Company* (1893), 98 Cal. 184, 32 Pac. 945.

III.

THE USE TO WHICH THE TRACTOR WAS BEING PUT AT THE TIME AND PLACE OF THE ACCIDENT HERE INVOLVED WAS NOT A USE "FOR TRANSPORTATION OF MERCHANDISE PURPOSES" WITHIN THE MEANING OF THE POLICY, AND, ACCORDINGLY, LIABILITY COVERAGE DID NOT EXTEND TO THE TRACTOR AT THAT TIME AND PLACE.

Irrespective of who had the burden of proof or whether plaintiffs (appellants) made out a *prima facie* case, we submit that the evidence affirmatively shows that the vehicle was not covered at the time and place of the accident.

It is, of course, conceded that at the time of the accident in question the assured "physically * * * wasn't carrying merchandise" (concession by plaintiffs' counsel, Tr. 119).

It is the contention of the Appellants (quite apart from the question of the burden of proof) that the use to which the vehicle in this instance was being put constituted "transportation of merchandise" within the meaning of the policy and counsel cites (App. Op. Br. pp. 33-39) cases in which it is held that liability

coverage will extend if the use to which the vehicle was being put is an immediate incident of the purpose or use described in the policy.

The trial Court in its opinion (Tr. 59) refers to this class of cases, and approves them, as do we.

However, where as here, the use is "*totally unrelated to the use or the physical incident which resulted in the accident * * * liability does not exist*", as pointed out in the opinion of the learned trial judge (Tr. 59).

As stated in Judge Yankwich's opinion (Tr. 61):

"the use of a portion of the insured equipment, the truck part, to return to the place of origin, San Francisco, 250 miles away, *not* for the purpose of picking up a new load, or beginning a new haul, or storing or repairing the truck, *but for the purpose of paying a premium on an insurance policy on the truck, is not an act incidental to the transportation of goods on the truck or trailer.* Nor, for that matter, is the soliciting of business an incidence of such transportation. To be accessory to the business in which the truck was used, it would have to be covered by a policy which, either did not include any limitation, or insured generally against *any act or acts of the defendant while engaged in trucking for hire.* But the policy here under consideration *was not so comprehensive.* The defendant did not insure against all the risks of the plaintiffs while engaged in the business of trucking, but only against a specific risk. Otherwise put, it insured the automobiles when '*used only for transportation of merchandise purposes.*'"

We have searched in vain (understandably) for any case which has held, or even in which the claim has been made, that "transportation of merchandise" includes the use of a vehicle for driving 250 miles to pay a premium on an insurance policy, even though (assuming it to be the fact) the assured had, as an added purpose, an un-consummated and wholly unresolved "secret intent" to communicate with a prospective customer about future hauling operations, but intended all the while to return to his point of origin (the Eureka area) before embarking on such subsequent hauling operations.*

However, we submit that, by analogy, the following cases establish that the use to which the vehicle in this instance was being put was not a use for transportation of merchandise within the meaning of the policy.

In *State Compensation Insurance Fund v. Bankers Indemnity Insurance Company* (C. C. A. 9, 1939), 106 Fed. (2d) 368, this Court was confronted with a somewhat similar claim. The defendant insurance company in that case had issued a liability policy which provided that "the Company shall not be liable * * * for * * * claims arising from the use of any automobile for purposes other than those specified in the Declaration", which, in turn, provided that "the business of the Assured is hauling dirt for the City of Oakland" and that "the purposes for which the de-

*We discuss in the appendix to this brief the evidence and what it shows with respect to the use of the vehicle at the time of the accident.

scribed automobiles are and will be used are: commercial use * * *

The term "commercial use" was defined as "usual to the business of the named assured as described above, including loading and unloading of goods."

The assured was under a contract to furnish a truck and driver to, and to haul dirt and men for, Alameda County.

One of the men being carried by the assured on the job was injured, and his compensation carrier sought to compel the assured's liability carrier to indemnify the compensation carrier for funds laid out by it in respect of the injuries.

Judgment went for the defendant liability insurance carrier and, as one of its specifications of error, the compensation carrier urged that the vehicle "was being used by the assured in a commercial use, usual to the business of assured of hauling dirt including the loading and unloading thereof."

In affirming judgment for the defendant insurance carrier, this Court stated: "Appellants argue that the transportation of the workers was *incidental* to the business at hand and was permissible under the policy * * * The Policy states that the business of the insured is that of hauling dirt. At the time the policy was issued Dalton [the assured] was employed for that purpose by the City of Oakland. At that time it was not part of his employment to transport men to or from work. In fact, as he testified, it never had been part of his duties to carry workmen in con-

nection with his employment except on this road work where the accident occurred. So far as the transportation of workmen in his truck having been usual or incidental to Dalton's business at, or prior to, the time of the issuance of the policy, the evidence is to the contrary and the finding of the trial Court in this regard must be sustained."

In *Commercial Standard Insurance Company v. Bacon* (C. C. A. 10, 1946), 154 Fed. (2d) 360, coverage was provided "on any motor vehicle operated or used for the transportation of freight or express, or both." An injury occurred while the vehicle was in a shop undergoing repairs, and the Court held that coverage did not extend. The case is of particular interest because in its opinion the Court refers with approval to *Mawhinney v. Southern Insurance Company* (1893), 98 Cal. 184, 32 Pac. 945. In that case recovery was sought on a fire policy which extended coverage to a harvester while "operating in the grain fields and in transit from place to place in connection with harvesting." The Supreme Court of California held that destruction by fire while the harvester was undergoing repairs in a blacksmith shop was not included in the coverage provided, and that the defendant insurance company should have been granted a non-suit at the close of plaintiff's case.

In *Farm Bureau etc. Insurance Company v. Daniel* (C. C. A. 4, 1939), 104 Fed. (2d) 477, liability coverage was provided, subject to the clause that the purposes for which the automobile was to be used were "hauling auto parts, building material and farm produce." The occupation of the assured was given as

“auto dealer and farmer.” It appeared that in connection with his automobile business the assured conducted a garage, and that at the time of the accident in question the vehicle described in the policy was being used for the purpose of carrying wrecked auto parts from the scene of an accident back to the garage operated by the assured. The Court held that liability arising out of an accident on such a trip was not covered.

In *C. E. Carnes & Co. v. Employers etc. Corporation*, (C. C. A. 5, 1939), 101 Fed. (2d) 739, liability coverage was provided the assured in the business of “Handling Farm Machinery, Crain Fixtures, and Paints.” The Court held that this policy did not provide coverage where the accident occurred while the vehicle was hauling Butane gas.

In *General Tire Co. v. Standard Accident Insurance Co.* (C. C. A. 8, 1933), 65 Fed. (2d) 237, the policy in question provided liability coverage for certain vehicles to be used “only for commercial purposes, excluding car use and towing”. The principal use described in the policy was for “checking air and inflating tires on various fleet accounts”. The Court held that no coverage was provided for an accident which occurred while the vehicle was being used to carry a tire and tube mounted on a spare wheel, even though the same was being delivered to one of the assured’s regular customers.

In *Duke Anderson Drilling Co. v. Smith* (1943), 193 Okla. 107, 141 Pac. (2d) 565, judgment notwithstanding the verdict was affirmed in favor of the

defendant insurer. The policy there in question provided "the automobile will be principally * * * used * * * for transportation and delivery of merchandise for compensation." At the time of the accident the vehicle was being used to pull another truck onto the highway after it had run into a ditch. The Court held that this was not a use covered by the policy.

See also the authorities cited in footnote 24 of Judge Yankwich's opinion (Tr. 73).

Numerous additional authorities can be cited to the same effect. See the following:

Williams v. American Automobile Insurance Co. (C. C. A. 5, 1930), 44 Fed. (2d) 704: hauling Boy Scouts was held to be not a "commercial purpose"; the Court stated: "Any incidental benefit or good will that might result from its use in an attempt to curry favor with an employee of the city water works is too remote to support the inference that such use was for commercial use."

Manthey v. American Automobile Insurance Company (1941), 127 Conn. 516, 18 Atl. (2d) 397: an insuring clause providing for coverage for "transportation or delivery of goods, merchandise or other materials and uses incidental thereto in direct connection with the insured's business", which was stated to be that of a dairy farmer, was held not to cover an accident which occurred while the assured's nephew was returning from having delivered a chicken to a customer.

Euto v. American etc. Casualty Co. (1936), 247 App. Div. 613, 288 N. Y. S. 232: a clause providing

coverage for any "commercial use * * * usual to the business of the named insured", which was that of a sand and gravel dealer, was held not to include an accident which occurred while the insured truck was being used in highway snow removal operations.

See also the following cases:

Hoar v. Gray (1945), 352 Pa. 373, 42 Atl. (2d) 822;

Bohnsack v. Huson-Ziegler Co. (1933), 212 Wisc. 65, 248 N. W. 764;

Snyder v. Natl. Union Ind. Co. (C. C. A. 10, 1933), 65 Fed. (2d) 844.

The analogies afforded by the above cases, we submit, demonstrate that the use of the vehicle in the instant case was not covered by the policy here involved.

IV.

THE STATUTORY ENDORSEMENT AFFIXED TO THE POLICY UNDER THE HIGHWAY CARRIERS' ACT AND THE RULES AND REGULATIONS OF THE PUBLIC UTILITIES COMMISSION (FORMERLY THE RAILROAD COMMISSION) CANNOT SERVE AS THE PREDICATE FOR ANY CLAIM OF COVERAGE, IN VIEW OF THE FACT THAT AT THE TIME AND PLACE OF THE ACCIDENT IN QUESTION THE VEHICLE WAS NOT BEING USED AS A COMMON CARRIER, OR FOR ANY PURPOSE DESCRIBED IN THE POLICY, OR FOR WHICH ANY PERMIT OF THE RAILROAD COMMISSION WAS REQUIRED, OR IN RESPECT OF WHICH SUCH ENDORSEMENT HAD ANY APPLICATION.

It would unduly prolong this brief to develop at length the proposition stated in the heading.

Judge Yankwich's opinion (Tr. 61-65) covers the point with clarity. See particularly the following portion (Tr. 61-62):

“The Railroad Commission rider attached to the policy, which is reproduced in the margin, did not enlarge on the coverage. Its aim, as I stated at the argument, was to protect the public against certain defenses arising from violations of the law by employees, lack of authorized use and the like, which might defeat liability. It did not, and could not, change a coverage limited to *a specific use* to a general coverage of the truck, *regardless of the use.*”

The opinion discusses and quotes *Foster v. Commercial Standard Ins. Co.*, 121 Fed. (2d) 117 (C.C.A. 10, 1941), which this Court approved in *Associated Indemnity Co. v. Bunney*, 137 Fed. (2d) 1 (C.C.A. 9, 1942).

See also: *Hawkeye Casualty Co. v. Halferty*, 131 Fed. (2d) 294 (C.C.A. 8, 1942), and *Simon v. American Casualty Co.*, 146 Fed. (2d) 208 (C.C.A. 4, 1944), which are cited in Footnote 24 of the Opinion (Tr. 73), and see the additional cases cited in that Footnote.

V.

AS THERE WAS NO SUBSTANTIAL CONFLICT IN THE EVIDENCE, AND NO SUBSTANTIAL EVIDENCE ON WHICH JUDGMENT IN FAVOR OF PLAINTIFFS (APPELLANTS) COULD BE SUSTAINED, THE TRIAL COURT WAS CORRECT IN GRANTING JUDGMENT FOR DEFENDANT (APPELLEE) NOTWITHSTANDING THE VERDICT.

In their account of the facts developed at the trial (App. Op. Br. pp. 6-9) appellants have set forth (presumably) their most favorable view of the evidence developed at the trial.

We submit that a reading of appellants' statement demonstrates that the evidence is without substantial conflict and shows affirmatively (irrespective of who had the burden of proof or whether a *prima facie* case had been established) that at the time of the accident the vehicle described in the policy was not being put to any use for which liability coverage was provided in the policy. See also the appendix to their brief.

Appellants, at one point in their brief (App. Op. Br. p. 32) have even sought to make it appear that at the time of the accident Warner was on a normal return trip after having delivered cargo for compensation. This statement overlooks the undisputed testimony of the assured as to the use being made of the vehicle at the time of the accident. There is no evidence whatsoever that the assured was merely on a normal return journey from a carrier run. The evidence, as set out in appellants' opening brief (pages 6-9) and in the appendix to this brief, precludes any such claim.

Appellants (App. Op. Br. p. 34) pose the rhetorical question "Does the liability of the defendant turn on his [the assured's] secret intent or on his overt acts as found by the jury?". At the same time that appellants object to any inquiry as to the "secret intent" of the assured, they place great weight on the assured's (claimed) secret intent to communicate with Dowdell with regard to subsequent carrier operations. Thus, appellants' objection to any inquiry as to the assured's intentions on the trip when the accident occurred is inconsistent and merely serves to demonstrate that appellants' objection to any inquiry as to the intent of the assured is without merit.

Finally, although a normal return journey from a carrier run might well have brought the accident here in question within the ambit of the coverage clause, the evidence shows without substantial conflict that at the time when the accident occurred the assured was not engaged on a return journey from a carrier run.

Under these circumstances we submit that it was not only proper but requisite that the trial Court direct a verdict in favor of the appellee.

The general rules covering directed verdicts are well known to this Court.

As stated in *Perumean v. Wills* (1937), 8 Cal. (2d) 578, 67 Pac. (2d) 96, in which the Court quoted from *Estate of Baldwin* (1912) 162 Cal. 471; 123 Pac. 267:

" 'A directed verdict is proper, unless there be substantial evidence tending to prove in favor of plaintiff all the controverted facts necessary to

establish his case. In other words, a directed verdict is proper whenever, upon the whole evidence, the judge would be compelled to set a contrary verdict aside, as unsupported by the evidence. To warrant a court in directing a verdict, 'it is not necessary that there should be an absence of conflict in the evidence, but, to deprive the court of the right to exercise this power, if there be a conflict, it must be a substantial one.' " (8 Cal. (2d) 581.)

In this connection we point out that the "scintilla of evidence rule" has been rejected in this jurisdiction. See *Walters v. Bank of America* (1937) 9 Cal. (2d) 46, 69 Pac. (2d) 839, and *DeZon v. Amer. Pres. Lines* (C.C.A. 9, 1942) 129 Fed. (2d) 404; affirmed, 318 U.S. 660 (1943).

And see: *Galloway v. U. S.* (1943) 319 U.S. 372, where the Supreme Court, in affirming judgment on a directed verdict for the defendant, stated:

"the essential requirement is that mere speculation be not allowed to do for probative facts, after making due allowance for all reasonably possible inferences favoring the party whose case is attacked." (319 U.S. 395.)

Connelly v. U. S. (C.C.A. 5, 1941), 123 Fed. (2d) 1:
 "Evidence which does no more than open the door to speculation is not sufficient to support a verdict * * * The trial court properly directed a verdict for the defendant."

Alexander v. Standard Accident Ins. Co. (C.C.A. 10, 1941) 122 Fed. (2d) 995:

* * * "The mere choice of probabilities does not constitute evidence and will not be submitted to the jury. Nor does the placing of inference on inference or presumption on presumption constitute a sufficient basis for the determination of facts."

We submit that under the rule of the above cases the action of the trial Court was proper.

VI.

THERE IS NO MERIT IN THE SUGGESTION MADE BY THE PLAINTIFFS (APPELLANTS) THAT THE ORDER OF THE TRIAL COURT DENYING DEFENDANT'S (APPELLEE'S) MOTION TO DISMISS PRECLUDED THE COURT FROM THEREAFTER GRANTING A JUDGMENT FOR DEFENDANT NOTWITHSTANDING THE VERDICT.

Appellants argue in their brief that a directed verdict cannot be granted "upon evidence offered by a defendant after a plaintiff has first established a *prima facie* case" (App. Op. Br. p. 25, et seq.).

This statement is not in accord with the law controlling in this case (quite apart from the fact, as we have shown, that appellant failed to make out a *prima facie* case).

As stated in 24 *Cal. Jur.* 916, "Trial", sec. 163:

"And the fact that the court has denied a motion for a nonsuit will not prevent it from subsequently directing a verdict for the defendant when the condition of the evidence so warrants. An order directing a verdict will not be reversed on appeal unless the trial court has abused its discretion."

In *Arthur v. London Guarantee and Accident Co.* (1947), 78 Cal. App. (2d) 198, 177 Pac. (2d) 625, a liability insurance carrier defended an action in which its assured sought to compel it to pay a judgment against the assured. The insurance carrier defended on the grounds that the plaintiff had failed to give notice as required by the policy. There was evidence that the assured had sent photographs of the accident to its broker. The Court held that it could not be presumed "from this set of facts that the insurance company had received notice of the accident." At the conclusion of the plaintiff's case a *motion for nonsuit was denied*. At the conclusion of defendant's case a *motion for directed verdict was denied*. The jury returned a verdict for plaintiff. Thereafter the trial Court *granted the defendant's motion for judgment notwithstanding the verdict*, and that order and judgment were affirmed on appeal.

See also *Sellers v. Solway Land Co.* (1916), 31 Cal. App. 259 at 269, 160 Pac. 175, and *Fuchs v. Southern Pacific Co.* (1935), 5 Cal. App. (2d) 409 at 412, 42 Pac. (2d) 704, where the Court stated:

"the settled rule is that the fact that a motion for a nonsuit has been denied does not prevent the court from subsequently directing a verdict for the defendants. (24 Cal. Jur. 916.)"

VII.

THE TRIAL COURT COMMITTED ERROR PREJUDICIAL TO APPELLEE WHEN IT (a) DENIED APPELLEE'S MOTION FOR DISMISSAL UNDER RULE 41-b AT THE CONCLUSION OF APPELLANTS' CASE, (b) DENIED APPELLEE'S MOTION TO SET ASIDE THE ORDER STRIKING THE PLEA OF RES JUDICATA, AND (c) DENIED APPELLEE'S MOTION FOR A NEW TRIAL, IN THE ALTERNATIVE, SO CONDITIONED THAT THE ORDER GRANTING SUCH NEW TRIAL WOULD BECOME EFFECTIVE ONLY IN THE EVENT THAT THE JUDGMENT NOTWITHSTANDING THE VERDICT SHOULD BE REVERSED ON APPEAL.

After the verdict, defendant renewed its motion for a directed verdict and moved the Court for judgment notwithstanding the verdict and, in the alternative, for an order granting a new trial, so conditioned that such order should become effective only in the event that the judgment notwithstanding the verdict should be reversed on appeal (Tr. 48-51). The motion for judgment notwithstanding the verdict was granted but the alternative motion for new trial was denied (Tr. 51).

We do not anticipate that the Court will reverse the judgment in this case.

However, in order to forestall any claim that we have abandoned our position, we hereby assign as error the three rulings referred to in the heading.*

Our authority for seeking here a review of these rulings is *Montgomery-Ward Co. v. Duncan* (1940), 311 U.S. 243, 85 L.Ed. 547, where the Court stated:

*If the judgment is affirmed, it is obvious that the points here referred to will become moot.

“If the trial judge, as he did here, grants judgment n. o. v. and denies the motion for a new trial, the party who obtained the verdict may, as he did here, appeal from that judgment. Essentially, since his action is subject to review, the trial judge’s order is an order nisi. The judgment on the verdict may still stand, because the appellate court may reverse the trial judge’s action. This being so, we see no reason why the appellee may not, and should not, cross-assign error, in the appellant’s appeal, to rulings of law at the trial, so that if the appellate court reverses the order for judgment n. o. v. it may pass on the errors of law which the appellee asserts nullify the judgment on the verdict”.

In reference to the opinion just quoted it is suggested in “Federal Rules of Civil Procedure with Approved Amendments”, 1947 Revised Edition, published by West Publishing Co. (p. 395):

“When the Supreme Court uses the words ‘cross-assign error’, it is to be assumed that the old form of assignments of errors is not contemplated since that was abolished by Rule 75, except in the case where the appellant does not designate the complete record for review in which event a statement of the points to be relied upon must also be filed. Probably all that should be required of the appellee is a statement in his brief that on the appellant’s appeal he will also raise the counter-points set forth in his appellee-brief.”

(a) The trial Court committed error prejudicial to appellee when it denied appellee's motion for dismissal under Rule 41-b (F. R. C. P.) at the conclusion of appellee's case.

After introducing in evidence, as part of their case in chief, the insurance policy upon which they are here seeking to recover (Ptf's Exhib. #1, Tr. 88 et seq.), plaintiffs wholly failed to introduce any evidence whatsoever respecting the use to which the vehicle was being put at the time and place of the accident in question.

At the conclusion of plaintiffs' case defendant (appellee) moved for a dismissal under the provisions of Rule 41-b (F. R. C. P.) on the ground that plaintiffs, after completing the presentation of their evidence, had not shown any right to relief (Tr. 95). This motion was denied (Tr. 97).

For the reasons set out under points I and II (supra), the ruling by which the trial Court denied the motion to dismiss was erroneous.

That the error was prejudicial to appellee was, we submit, clear: appellee was required to proceed, after plaintiffs rested, with proof of matters which were part of plaintiffs' case; the tactical disadvantage to which appellee was put is, we submit, obvious; plaintiffs should have been required to prove all of the elements of their cause of action, and as they had failed to do so when they rested, their action should have been dismissed.

- (b) The trial Court committed error prejudicial to appellee when it denied appellee's motion to set aside the order striking the plea of *res judicata*.

In paragraph VII of its answer (Tr. 13-21), defendant (appellee) pleaded the defense of *res judicata*, based upon judgments in the declaratory relief action by which Judge Goodman had declared (after listening to Warner testify) that the accident here involved was not covered by the policy here in question. The assureds, Warner and Woodrow, were served with process in the declaratory relief action and defaulted. The plaintiffs in the personal injury action (plaintiffs and appellants here) were not served with such process (Tr. 67).*

Nevertheless, it was and is the contention of appellee that the adjudication of non-coverage was binding upon appellants and that the order striking the defense of *res judicata* and the order of the trial Court in refusing to permit such defense to be reinstated (Tr. 98-99) were erroneous.

It is hardly necessary to point out that in an action of this type "the injured person has the same right against the insurance carrier as the insured would have, and that a defense good against the insured is good against the injured claimant," (*Sears v. Illinois Indemnity Company* [1932], 121 Cal. App. 211 at 224, 9 Pac. [2d] 245), and that "the injured person stands in no better position than the assured" (*Valladao v. Firemen's Fund Indemnity Co.* [1939], 13 Cal. [2d]

*Plaintiffs were well aware of the pendency of the declaratory relief action and had adequate opportunity to protect their interests in that litigation (see Defendant's Exhibit C, Tr. 183-184).

322, 89 Pac. [2d] 643. See also *Royal Ind. Co. v. Morris* [C.C.A. 9, 1929] 37 Fed. [2d] 90).

It is clear (we submit) that if the assureds had attempted, after the declaratory relief action, to sue the insurance company on the policy, the plea of *res judicata* based on the judgment in the declaratory relief action would have constituted a valid defense against the assureds. We submit that it is equally a valid defense against the plaintiffs and appellants here, since they stand in the shoes of the assureds.

The rules for determining the validity of a plea of *res judicata* were stated as follows in *Bernhard v. Bank of America* (1942) 19 Cal. (2d) 807 at 813; 122 Pac. (2d) 892: "In determining the validity of a plea of *res judicata* three questions are pertinent: Was the issue decided in the prior adjudication identical with the one presented in the action in question? Was there a final judgment on the merits? Was the party against whom the plea is asserted a party or in privity with a party to the prior adjudication?" (19 Cal. [2d] 813).

That the plea of *res judicata* made by the defendants in the instant action falls squarely within the requirements laid down in the *Bernhard* case is, we submit, manifest: (i) the issue of coverage was squarely determined in the action for declaratory relief; (ii) the judgment in the declaratory relief action was a final judgment on the merits on the question of coverage, and (iii) the party against whom the defendant in this case asserted the plea of *res judicata* is "in privity with a party to the prior adjudication".

That the assured in a liability policy and a person injured by his negligence are in privity within the meaning of the rule above referred to is held in *Connold v. Stern*, 138 Oh. St. 352; 35 N.E. (2d) 133; affirmed in 67 Oh. App. 134; 36 N.E. (2d) 38 (1940).

In that case, it appeared that *Luntz* and *Connold* had been injured by the negligence of *Stern*, the assured. They recovered judgment against *Stern*, and thereafter *Luntz* brought an action against *Stern* (the assured) and his *liability insurance carrier*, which resulted in an adjudication of non-coverage. *Connold*, who was not a party to that proceeding, thereafter brought an action against the liability insurance carrier, and it was held that the adjudication of non-coverage was binding on *Connold*, even though he was not a party to the proceeding in which the adjudication was made. The Court noted that *Connold's* action was derivative, and stated:

“* * * the right of Stern [the insured] against the insurer cannot be relitigated. His right against the insurance company was fully litigated in the former supplemental action and the judgment against him in that case stands as a bar for all time. Restatement of Judgments (tentative Draft No. 1), 130, Section 330. Must it not be a bar against any third party whose right, if any, against the insurance company is derived from and dependent upon a valid right of Stern [the insured] against the insurance company. * * * *Res judicata* or estoppel operates not only between parties to an action but between parties, and others not parties, as to the derivative rights of the latter which flow from those who were adversary parties in the action.”

The relationship between the assureds (Warner and Woodrow) and the plaintiffs in this action was clearly stated by plaintiffs' counsel when he wrote to the assureds, Warner and Woodrow, on December 4, 1946 (Def.'s Ex. C, Tr. 183-184) and called their attention to the pendency of the declaratory relief action and pointed out that his clients (plaintiffs in the instant action) as well as Warner and Woodrow, were named defendants in the declaratory relief action, and stated "*there is a unity of interest between us*" (Tr. 184).

In view of the rules above set out, we submit that the plea of *res judicata* should have been allowed to stand.

(c) The trial Court committed error prejudicial to appellee when it denied appellee's motion for a new trial, in the alternative, so conditioned that the order granting such new trial would become effective only in the event that judgment notwithstanding the verdict should be reversed on appeal.

We have pointed out under sub-headings (a) and (b) errors of law committed on the trial of the action.

In the remote contingency that this Court should hold that Judge Yankwich erred in granting judgment notwithstanding the verdict, we respectfully submit that, in view of the errors of law above referred to, appellant would be entitled, in such alternative, to a new trial. See *Montgomery-Ward & Co. v. Duncan*, pp. 27-28, *supra*.

VIII.

CONCLUSION.

In conclusion, it is respectfully submitted that the judgment notwithstanding the verdict should be affirmed, and that if this Court should hold otherwise, a new trial should be allowed.

Dated, San Francisco, California,
February 16, 1949.

Respectfully submitted,
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(Appendix Follows.)

Appendix.

Appendix

REFERENCES TO RECORD WHICH SHOW PURPOSE OF WARNER IN MAKING TRIP ON WHICH ACCIDENT OCCURRED.

Two days after the accident, in his report to the insurance company (Def's. Ex. B, Tr. 175-178), dated *June 24, 1946*, the assured Warner reported (*inter alia*):

"My wife June was riding in the cab with me at the time. The accident occurred about two (2) miles south of Scotia, Calif., on Highway No. 101. I had no cargo at the time. I was returning from Willow Creek, Calif. I had taken my mother and son there to visit my sister at Willow Creek."

On *August 8, 1946*, the plaintiffs (appellants) in the instant action filed a personal injury action against the assureds, Warner and Woodrow (Tr. 5), and on *August 26, 1946*, the insurance company (appellee here) and Warner and Woodrow executed (Def's. Ex. A, Tr. 159-160) a reservation of rights agreement under which the insurance company assumed the defense of the personal injury action.

On *October 18, 1946*, in the U. S. District Court in San Francisco (Tr. 13) the insurance company (defendant and appellee in this action) filed an action for declaratory relief in which it sought an adjudication of non-coverage as against its assureds and also as against the plaintiffs in the personal injury action

and in this action. (The latter were not served in the declaratory relief action.)

On *August 11, 1947*, the declaratory relief action came on for hearing before Judge Goodman in the District Court in San Francisco, on Warner's default (Tr. 15), and at that time Warner testified that he had gone up to Willow Creek (which is near Eureka) and that (Tr. 156) he "had intended, if possible, to haul barrels out of Willow Creek", although he saw no one about this (Tr. 156). The principal purpose mentioned by him to Judge Goodman respecting the trip up to the Eureka area was in the nature of a vacation purpose (Tr. 156-158).

In *September of 1947*, the personal injury action came on for trial in the Superior Court in San Francisco, and Warner there testified (Tr. 188-193) that he had gone to Blue Lakes (a part of the Willow Creek-Eureka area) with a load of pipe on his trailer, that he had left the trailer there, that on the accident trip he was in the tractor, that his destination at the time of the accident was San Francisco, and that he intended to go back to the Eureka area to get the trailer (Tr. 191).

Warner was then asked (we are still speaking of his testimony in the State Court in September of 1947) the purpose of the trip to San Francisco, on which the accident occurred (Tr. 193):

"Q. (by Mr. Gray, appellants' counsel in the State Court case and this case). Were you returning back to continue with your business?

A. (by Warner). No, I had a definite purpose in coming down, I might state. I had a payment due on my insurance policy Monday. My policy would lapse if I did not get in here Monday. That was the reason for coming down to Frisco here.

Q. So you came down for that business?

A. That's right.

Q. And when did you intend to go back for your trailer?

A. The following day."

In the trial of the instant case there was no material departure from the accounts previously given by Warner.

On direct examination in the instant case Warner testified as follows concerning his purposes in making the trip on which the accident occurred (Tr. 110-111):

"Q. Now what was your purpose in going to San Francisco?

A. There was an installment due on the policy, this policy. It was due on a Monday morning, or it was due, anyway—I forget how many hours I had grace, but that was my reason for coming to San Francisco as I did, without the trailer."

The accident happened on this trip; Warner continued on to San Francisco, reported the accident to the insurance company, paid the premium, and returned to Eureka to get his trailer, and then came back to San Francisco for the second time (Tr. 114-115).

At this juncture in the trial, Judge Yankwich asked Warner (Tr. 115):

“Q. Well did you pick up your trailer, and the pipes then unloaded from your trailer?

A. Everything had been unloaded. I had a haul at the time with John Dowdell, of San Jose. That is John Dowdell, Draymen; I believe we were hauling concrete pipe out of San Jose for housing projects all over the area, the peninsula area. That was one of the * * *

Q. Well the point is this; you came back empty?

A. Yes.”

(This return trip, of course, refers to the trip from the Eureka area to San Francisco which occurred *after* the trip on which the accident happened.)

On cross-examination (in the instant case), counsel for the plaintiffs asked (Tr. 127):

“Q. * * * Now you testified that you also came down to discuss with someone in San Jose the hauling of a load, is that true?”

There had been, up to the time of counsel’s question, no such testimony, but the witness nevertheless answered in the affirmative (Tr. 127) and stated that that was one of his purposes in making the trip on which the accident occurred, although he neither saw nor communicated with Dowdell (Tr. 139).

Although the assured, Warner, might well have given a more complete report of the circumstances surrounding the accident when he gave his original

report to the insurance company (Def. Ex. B), he fully explained this by stating that it had not occurred to him that his purposes in making the trip on which the accident happened had any bearing on the subject of insurance, and that, accordingly, he had not included in his original report certain details of the trip which he brought out at subsequent dates (Tr. 129-132).

As stated in Judge Yankwich's opinion (Tr. 57-58):

"In these statements, made shortly after the accident, the aim of the trip was given as a vacation for his mother, wife, and himself. He claimed that the reason for the omission of the fact that he was carrying the pipe and the household goods was that he thought it unimportant. He admitted, however, that he began to think about the possible significance of the transportation feature of the trip, when, in talking to other truck operators, they reminded him that this transportation might have a bearing upon the liability insurance which he carried. One fact stands out in this narrative: The main purpose of the return trip was made to pay the premium. This main purpose was, in fact, the sole purpose, because we cannot consider any intention not carried into effect, such as solicitation of business."

No. 12,056

IN THE
United States Court of Appeals
For the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA
L. BOULTER,

Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Appellee.

Appeal from the United States District Court for the
Northern District of California, Southern Division.

APPELLANTS' REPLY BRIEF.

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FILED

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PAUL R. O'BRIEN,

CLERK

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APPELLANTS' REPLY BRIEF.

In our opening brief, page 14, we stated that the admissions in the pleadings, the evidence, and the stipulation of counsel establish *every fact alleged in the complaint*. The defendant in its brief at the outset appears to take issue with this statement, but ultimately tacitly concedes it by admitting that the answer to the question of upon whom rested the burden of proving that the tractor was not being used for transportation of merchandise purposes is determinative as to whether plaintiffs established a *prima facie* case. (Appellee's Br. p. 4.)

The question as to upon whom rested the burden of proving this point depends on whether or not the provisions of the policy relating thereto constitute a condition precedent or a condition subsequent, and can only be determined after considering all of the provisions in the policy and the endorsements attached thereto.

I.

UNDER THE TERMS OF THE POLICY THE USE OF THE VEHICLE WAS NOT A CONDITION PRECEDENT.

Before discussing the provisions of the policy that are applicable to this question, attention is directed to the rule relating thereto that was enunciated in the case of *Neilson v. American Mut. Liability Ins. Co.*, 111 N.J.L. 456, 168 A. 436. In that case the policy provided "that the Company would not be liable if the vehicle was used for any purpose other than that specified in the declarations contained in the policy".

"Insurance contracts, as a rule, contain both affirmative and promissory warranties. The first class relates to matters existing at or before the issuance of the policy, and has the effect of a condition precedent; while a promissory warranty is one where the insured stipulates that something shall be done or omitted after the policy takes effect, and during its continuance, and has the effect of a condition subsequent. The provisions now under consideration must be construed as promissory warranties on the part of the insured, and in the nature of conditions subsequent,

a compliance with which is essential to the right of recovery under the contract.”

See also:

Beatty v. Employers' Liability Assur. Corp.,
Supreme Court of Vt., 1933, 106 Vt. 65, 168
A. 919.

That there is a conflict in the decisions of various jurisdictions regarding what are conditions precedent and conditions subsequent is recognized in the case of *O'Morrow v. Borad*, 27 Cal. (2d) 794, 800 (167 P. (2d) 483).

Aside from the effect of the provisions of the endorsement attached to the policy that was prescribed by the Railroad Commission of the State of California, which is hereinafter discussed, those provisions of the policy that relate to this subject are as follows:

Under the title, “**Declarations**”, appears the following: “5. The Automobiles described are and will be used only for transportation of merchandise purposes and will be operated as follows, and this insurance covers for no other use or operation:” (Tr. p. 25.)

The insuring agreements contain the usual indemnity agreements, and on this subject state: “**VI. Policy Period, Territory, Purposes of Use.** This policy applies only to accidents which occur during the policy period, while the automobile is within the United States of America, and is owned, maintained and used for the purpose stated as applicable thereto in Statement 5 of the declarations.” (Tr. p. 35.)

Immediately following, under the title, "**Exclusions**", it is provided: "This policy does not apply:" Then follows, among other things, certain uses of the automobile, such as using it for transportation of persons for consideration, renting, leasing, or hiring it, or towing a trailer not covered by like insurance in the company. (Tr. pages 35-36.)

Under the title, "**Conditions**", appears the following: "14. Declarations. By acceptance of this policy the named insured agrees that the statements in the **Declarations** are his agreements and representations, that this policy is issued in reliance upon the truth of such representations and that this policy embodies all agreements existing between himself and the company or any of its agents relating to this insurance." (Tr. p. 42.)

The defendant does not question the authoritative value of the cases which we cited holding that the burden is on the insurance company to prove facts which bring into operation an exception to general coverage or a condition subsequent. (Appellee's Br. p. 11.) It contends, however, on the same page that these cases are not applicable because here the only coverage provided is on a vehicle while "used only for transportation of merchandise purposes", and emphasizes that this declaration further provides that "this insurance covers for no other use or operation."

Apparently the defendant concedes that if the provision under consideration were in the policy under the title, "**Exclusions**", the provisions of which are

prefixed by the words, "This policy does not apply:", a different rule would then prevail. Without invoking at this point the fundamental rule of construction which favors the insured, the distinction that the defendant makes must rest upon the location in which the declarations appear in the policy or the connotation derived from the word, "declarations", as distinguished from the location and connotation of the word, "exclusions".

The purported exception from the operation of the policy under both titles is unambiguous and attains the same objective. Under the title, "Declarations", it is provided that the "insurance covers for no other use or operation", whereas under the title, "Exclusions", it is provided: "This policy does not apply:". Obviously under either clause the insurer escapes liability if the facts under either provision are established, subject only to the effect of the Railroad Commission endorsement.

"Stipulations in a contract are not construed as conditions precedent, unless that construction is made necessary by the terms of the contract." (*Deacon v. Blodget*, 111 Cal. 416, 418, 44 P. 159.) In considering conditions precedent generally, the Supreme Court of the State of California stated: "* * * it is well settled that such conditions are not favored by the law, and are to be strictly construed against one seeking to avail himself of them." (*Antonelle v. Lumber Co.*, 140 Cal. 309, 315, 73 P. 966.) In applying this doctrine to insurance contracts, the same court stated:

“ ‘The rule of law is that policies are to be construed liberally in favor of the assured.’ (*Wells, Fargo & Co. v. Pacific Ins. Co.*, 44 Cal. 411.) ‘Any uncertainty or ambiguity in a contract of insurance is to be interpreted most strongly against the insurer.’ (*Goorberg v. Western Assur. Co.*, 150 Cal. 515 (119 Am. St. Rep. 246, 11 Ann. Cas. 801, 10 L.R.A. (N.S.) 876, 89 Pac. 132).) ‘*Courts are disinclined to construe the stipulations of a contract as conditions precedent, unless compelled by the language of the contract plainly expressed. The reason for this disinclination is that such a construction prevents the court from dealing out justice to the parties according to the equities of the case.*’ ” (Italics added.)

Victoria S.S. Co. v. Western Assur. Co., 167 Cal. 348, 353, 139 P. 807.

Moreover, if the provisions under consideration are susceptible to the construction contended by plaintiffs, and likewise to the construction contended by defendant, they must be construed strictly as against the insurer.

“This for two reasons: (1) Because it is found in a policy of insurance (Civ. Code, sec. 1654; *Maryland Casualty Co. v. Industrial Acc. Com.*, 178 Cal. 491, 494 (173 Pac. 993); *Wells Fargo & Co. v. Pacific Ins. Co.*, 44 Cal. 397); and (2) because the language in question is found in an exception, attached to the policy, which purports to limit the risk assumed by the insurer in the general provisions thereof. (*Berliner v. Travel-*

ers' Ins. Co., 121 Cal. 458 (66 Am. St. Rep. 49, 41 L.R.A. 467, 53 Pac. 918).)"

Mah See v. North American Acc. Ins. Co., 190 Cal. 421, 424-5, 213 P. 42.

Defendant cites a number of cases of other jurisdictions holding that where the policy limits the automobile to a particular use, this constitutes a condition precedent and imposes upon the plaintiffs the burden of proving that the use of the automobile at the time of the accident was one contemplated by the policy. We have not contended that the nature of the use could not be a condition precedent if appropriate language to this effect were used and it was susceptible to no other conclusion.

In determining who has the burden of proof, the rules adopted by the courts of California are controlling.

"The question of where the burden of proof lies is one of substantive law, as to which the local rule must be observed. (Citing cases.)"

New York Life Ins. Co. v. Rogers, C.C.A. 9th, 1942, 126 F. (2d) 784, 788.

Defendant cites the cases of *Allen v. Home Ins. Co.*, 133 Cal. 29 (65 P. 138), and *Arnold v. American Ins. Co.*, 148 Cal. 660 (84 P. 182), as supporting its contention. These cases merely hold that the provisions there under consideration were conditions precedent, and it was so concluded in the subsequent case of *Jones v. International Indemnity Co.*, 39 Cal. App. 706 (179 P. 692), wherein the court, in referring to those cases, stated:

“In the cases cited the complaints showed that there were certain conditions precedent, the performance of which was not alleged.”

Elsewhere in this brief we point out that the provision, “will be used only for transportation of merchandise purposes”, is modified by the Railroad Commission endorsement, in that this endorsement has the effect of making the defendant liable for accidents occurring while the insured was performing any function incidental to the operations of a motor carrier. We there show that the statutory definition of the operations of such carrier is much broader than the restriction in the declaration relied upon by defendant. When the provisions of the declaration are construed with the provisions of the endorsement, it becomes apparent that the former could not be a condition precedent even if the policy had so expressly provided; this for the obvious reason that the declaration is void to the extent that it purports to restrict the coverage of the policy and throw upon persons injured by the insured a greater burden than contemplated by the statutes to which the endorsement relates.

II.

THE JUDGMENT IS ERRONEOUS EVEN THOUGH THE COURT WERE TO HOLD THAT THE DECLARATION WAS A CONDITION PRECEDENT AND THAT THE PLAINTIFFS HAD THE BURDEN OF PROVING IT.

Assuming without conceding that the defendant's contentions are correct to the effect that the provi-

sions in the declarations were conditions precedent and that plaintiffs had the burden of proving that at the time of the accident the vehicle was being used for the purposes contemplated by the provisions of the policy, the same result would ensue. It is not to be overlooked that this is an appeal from a judgment in favor of the defendant notwithstanding a verdict of a jury in favor of the plaintiffs. The burden of proof is satisfied by actual proof of the facts of which proof is necessary, *regardless of which party introduces the evidence.* (*Aetna Ins. Co. v. Taylor*, 86 F. (2d) 225.) In *Estate of Burns*, 26 Cal. App. (2d) 741, 80 P. (2d) 77, the court, in discussing the power of the court to grant a nonsuit, stated:

“The expression, ‘disregarding conflicting evidence’, obviously means to disregard only the fact that there is a conflict in the evidence and give full credit only to that portion of the evidence, *whether produced by plaintiff or defendant*, which tends to support the allegations contained in plaintiff’s complaint.” (Italics added.)

(Pages 743-4.)

It is contended by defendant that the court committed prejudicial error in denying its motion for dismissal at the time that plaintiffs rested their case. If it be assumed that the denying of this motion was erroneous, it was, nevertheless, not prejudicial.

“The denial of a motion for a nonsuit is not prejudicial error where facts sufficient to support the judgment are in evidence either before or after the denial of the motion. (*Crosby v. Cline*, 186 Cal. 698 (200 Pac. 801).) Whether or not

denial of this motion was prejudicial error must depend upon our conclusions as to whether there was sufficient evidence to sustain the judgment."

Parra v. Cleaver, 110 Cal. App. 168, 170, 294 P. 6.

See also:

Peters v. Southern Pacific Co., 160 Cal. 48, 52-53, 116 P. 400;

Huston v. Schohr, 63 Cal. App. (2d) 267, 272-3, 146 P. (2d) 730.

In so far as the complaint is concerned, the allegation in paragraph II (Tr. p. 2) that Warner and Woodrow were at all times on the 22nd day of June, 1946 (the day of the accident), engaged in transporting property for hire as a business over public highways in the State of California by means of motor vehicles is sufficient to meet the objection of defendant. The modern philosophy concerning pleadings is that they do little more than indicate generally the type of litigation that is involved, and a generalized summary of the case that affords fair notice is all that is required. (*Securities and Exchange Commission v. Time Trust, Inc.*, D.C. Cal. 1939, 28 F. Supp. 34.)

Furthermore, any deficiency in the complaint relating to this point was cured by the answer of the defendant, which in great detail sets forth the provisions of the declaration and the alleged failure of its insured to comply with its provisions. (Tr. pp. 11-13.)

“While allegations of the performance of conditions precedent are essential to the statement of a cause of action upon a policy of insurance (*Allen v. Home Ins. Co.*, 133 Cal. 29 (65 Pac. 138); *Arnold v. American Ins. Co.*, 148 Cal. 660 (25 L.R.A. (N.S.) 6, 84 Pac. 182)), here appellant by its answer alleged that neither the plaintiff nor the insured had performed the terms and conditions of the policy, thus treating the issue as properly made, and curing the defect.”

Zimmerman v. Continental Life Ins. Co., 99 Cal. App. 723, 725-7, 279 P. 464.

In support of its contention that there is no evidence that the vehicle was being used for transportation of merchandise purposes, the defendant, in discussing the testimony of Warner, chooses to conclude that it would only sustain a finding that he was driving 250 miles to pay a premium on an insurance policy, and to consummate a wholly unresolved secret intent to communicate with a prospective customer about future hauling operations. (Appellee's Br., p. 15.)

No reference is made to the wildcatting operations of the insured, nor to the fact that regardless of his intent he was actually returning to his point of origin after having delivered property for compensation. This point was fully covered in our opening brief, and we at this time only call attention to the additional case of *Davis v. California Highway Indem. Exch.*, 118 Cal. App. 403 (5 P. (2d) 447). In that case the policy provided that the vehicle was to be used for “auto tours”. A real estate concern contracted with

the insured to furnish the automobile with a driver to bring passengers to a sightseeing bus. For this purpose the plaintiff became a passenger of the automobile, and when she arrived at the location from which the bus was to start it was decided that on account of unfavorable weather the trip would be abandoned. Upon returning the plaintiff to her home the accident occurred.

“These being the principal evidentiary facts in relation to the stated issue, appellant now contends that the evidence conclusively shows that the car was not being used in ‘auto tours’, but that plaintiff was merely a passenger in the ordinary sense of one who is a passenger in an automobile for hire. Wherefore it is argued that the court erred in finding that at the time of said accident said automobile was being used for auto tours and was covered by the indemnity policy. It may be conceded that at the time of the accident the automobile was being used under a contract hiring it for the stated purpose; but the evidence justified the court in finding further that said automobile under said contract of hiring was being used for touring purposes, and that under the arrangement made with the plaintiff her trip or tour of the day was to begin when she left her home and end when she was returned thereto.”

118 Cal. App. 403, 406-7, 5 P. (2d) 447.

Furthermore, even if it be assumed that the return to the point of origin to pay the insurance premium on the policy in question constituted a use of the vehicle not covered by the policy, this fact would not

in itself preclude plaintiffs from recovering, as the jury had the right to conclude from the evidence that Warner was also doing other acts within the purview of his customary operations as a carrier of property.

“ ‘If there is at the same time both an authorized and unauthorized use, the policy protects for liability arising from the latter as much as from the former use.’ ”

Johnson v. National Casualty Co., Court of Appeals, La. (1937), 176 So. 235.

This same doctrine has been followed in California.

“It has been held that when two causes join in causing an injury, one of which is insured against, the insured is covered by the policy.
* * *”

Zimmerman v. Continental Life Ins. Co., 99 Cal. App. 723, 726, 279 P. 464.

III.

THE DETERMINATIVE QUESTION IS NOT WHETHER THE INSURED WAS AT THE TIME OF THE ACCIDENT TRANSPORTING MERCHANDISE, BUT WHETHER HE WAS PERFORMING ANY OPERATIONS OF A MOTOR CARRIER.

The defendant places considerable reliance upon the case of *Foster v. Commercial Standard Ins. Co.*, 121 F. (2d) 117. Nothing in that case is in conflict with the position we have assumed here, in that there the “damage admittedly was incurred while the insured was operating the truck for pleasure and outside the coverage of the policy.” (page 120). It is note-

worthy that although in that case the policy had the same declaration as is here involved, namely that the truck "would be used only for transportation of merchandise purposes", the court, nevertheless, extended this provision under the corporation commissioner's endorsement to the *operations of a contract carrier*.

"The policy did not include coverage for loss from operations other than those of a *contract carrier*, nor did the permit require such coverage. * * * Plaintiff was not liable to respondent in damages for the loss suffered by defendants while the truck was being operated *other than in the business of assured as a common carrier*." (Page 120.) (Italics added.)

The endorsement required by the Railroad Commission and attached to the policy here involved provides:

"The policy to which this endorsement is attached is an Automobile Bodily Injury Liability and Property Damage Liability policy, and is hereby amended to assure compliance by the insured, as a *motor carrier of property*, with appropriate provisions of law (Highway Carriers' Act, Statutes 1935, Chapter 223, as amended; City Carrier's Act, Statutes 1935, Chapter 312, as amended; and Public Utilities Act, Statutes 1915, Chapter 91, amended); and with the pertinent rules, orders, and regulations of the Railroad Commission of the State of California.

"* * * that the right of any person, firm or corporation to recover under the policy shall not be affected by any act, omission, or misrepresentation of the insured or his employees with regard

to any warranty, condition, declaration, or provision of the policy; and that the policy shall remain in full force and effect notwithstanding such act, omission or misrepresentation or the violation of any warranty, condition, declaration or provision of the policy by the insured or his employees; Provided, However, that this endorsement shall not be construed to impose any obligation on the Company for which it would not be liable independently hereof with respect to * * *

(4) any loss arising out of any operations of the insured except operations authorized or for which authorization is required under the aforesaid statutes. * * *

“The Company further agrees that this endorsement shall prevail over any conflicting provision in the policy. * * *” (*Italics added.*)

(Tr. pp. 89-91.)

In the body of the policy itself it is provided: “Any specific statutory provision in force in the State in which this policy is issued shall supersede any condition of this policy inconsistent therewith.” (Tr. p. 41.)

“ ‘This policy having been issued for the express purpose of enabling the Johnson Company to comply with this statute, as the rider upon the policy shows, the provisions of the statute enter into, and become part of, the policy, and such statutory provisions override and supersede anything in the policy repugnant to such provisions.’ ”

Liberty Mut. Ins. Co. v. McDonald, 97 F. (2d) 497, 498.

Hence, in order to sustain the judgment notwithstanding the verdict in the instant case, it was not necessary for the jury to have determined whether or not the vehicle was being used for the transportation of merchandise at the time of the accident, *but whether it was being used for any operation of a motor carrier of property as defined by law and the specific statutes mentioned in the endorsement.*

The Highway Carriers' Act, Deering's California General Laws, Act 5129a (Sec. 1, subd. (f)), defines a highway carrier as every person "whatsoever engaged in transportation of property for compensation or hire as a business over any public highway in this state by means of a motor vehicle or motor vehicles."

Under the provisions of the Public Utilities Act "The term 'transportation of property', when used in this act, *includes every service in connection with or incidental to the transportation of property * * **" (italics added). (Deering's General Laws, Act 6386, Sec. 2, subd. (f).)

The activities of the insured also fall into the definition of a common carrier. "Everyone who *offers* to the public to carry persons, property, or messages, excepting only telegraphic messages, is a common carrier of whatever he thus offers to carry." (Italics added.) (*Civil Code*, Sec. 2168.)

In *Landis v. Railroad Commission*, 220 Cal. 470, 31 P. (2d) 345, the Supreme Court of California accepted a definition of a common carrier as stated in the case of *Sanger v. Lukens*, 24 F. (2d) 226.

“ ‘One who, by virtue of his calling and as a regular business, undertakes to transport persons or commodities from place to place, offering his services to such as may choose to employ him and pay his charges.’ This definition is particularly applicable to the petitioner Landis under the evidence. Within the limits of his equipment he holds himself out to haul what he offers to carry to those who may choose to employ him and pay charges satisfactory to him.”

(Page 474.)

In *Sanger v. Lukens*, *supra*, the court further stated:

“It then being clear that, when plaintiff undertakes for hire to transport upon the public highways of the state property for all who choose to employ him, he engages in the business of carrying and delivering commodities as a public employment, and is making the highways his place of business by using them as a common carrier.”

(Page 229.)

See also:

People v. Duntley, 217 Cal. 150, 163, 17 P. (2d)

715.

With these rules and definitions in mind, can it be seriously contended that the finding of the jury that Warner was using the vehicle in the performance of an operation of a motor carrier is “so lacking in evidentiary support that an appellate court would be impelled to reverse it upon appeal.” *Umsted v. Scofield Eng. Const. Co.*, 203 Cal. 224, 228, 263 P. 799. As previously pointed out, the fact that the insured may

also have been engaged in activities outside of those of a motor carrier is not determinative of the question.

Defendant has not contended that the "wildcatting" operations of its insured were not within the purview of the policy nor of the statutes applicable thereto. Hence, the question as to whether the insured was performing an operation of a motor carrier at the time of the accident must turn upon a consideration of what were his customary practices and activities in wildcatting. In its brief the defendant quotes testimony that it considers favorable to its contentions, and ignores the rule that upon an appeal from a judgment entered notwithstanding a verdict of a jury to the contrary, conflicting testimony and inferences must be ignored, and it is the duty of the court to consider only testimony and inferences that may be legally drawn therefrom which tend to support the verdict of the jury.

Aside from the fact that he was returning to his point of origin after delivering a cargo for compensation, Warner testified: that in wildcatting he has no definite over-the-road operation of his own, so he subhauls for big contractors (Tr. p. 103); that he does not always start from San Francisco, but may start from any place where he happens to be where he can locate a job (Tr. p. 129); that it was his intention to get a load out of Eureka for San Francisco, but at that time there was nothing coming out of that particular territory (Tr. p. 107); that while he was in the Willow Creek area he solicited business (Tr. pp.

112-113); that he intended if possible to haul barrels out of Willow Creek (Tr. p. 124); that at the time of the accident he was not on his vacation, and that one of his purposes in returning to San Francisco was to discuss with one Dowdell the hauling of a load (Tr. p. 127); that at the time of the accident he was on the most direct route to Dowdell's place of business in San Jose (Tr. p. 138); that it is customary in wildcatting to leave his trailer to be unloaded while he does something else (Tr. p. 129); that in wildcatting it is common practice to take a trailer that is already loaded instead of his own trailer, and that Dowdell has such trailers (Tr. p. 139); that there was nothing peculiar about his trip from Eureka to San Francisco, which was tied up with his intention to haul fruit for Dowdell, as fruit started to move at about that time of year (Tr. p. 167); that he had done a good deal of work with Dowdell in the past and had worked for him regularly (Tr. p. 166); and that although he intended to communicate with Dowdell he did not because the accident disabled his tractor. (Tr. pp. 139-140.)

This testimony clearly supports the implied finding of the jury that at the time of the accident Warner was wildcatting, and, consequently, performing an operation of a motor carrier.

In *Wood v. Vona*, 68 N. E. (2d) 80, a tractor was likewise involved in an accident, and it occurred while the tractor, after being repaired, was being driven to a place to get the trailer, and thence to go to a

place to resume hauling. The statutes of Ohio and the endorsement on the policy of that case are very similar to those here involved.

“Section 614-115, General Code makes it clearly apparent that the General Assembly intended to protect the public from loss or damage due to the operation of motor vehicles when operating under a permit granted by the Public Utilities Commission.

“If that purpose is to be attained, the policy must be given a broad and liberal interpretation in favor of the insured and those claiming under or through such insured.”

(Page 83.)

In that case, as in this, the endorsement provided:

“ ‘No condition, provision, stipulation, or limitation contained in the policy or any endorsement thereon, nor the violation of any of the same by the insured shall affect in any way the right of any person injured in person or property, within the state of Ohio, by negligence of the insured, *while* operating as aforesaid, or relieve the insurance company from the liability provided for in this endorsement or from the payment to such person of any judgment within the limits set forth in the policy, but the conditions, provisions, stipulations, or limitations contained in the policy or in any other endorsement thereon shall remain in full force and be binding as between the insured and the insurance company.’ * * *

“Ocean insists that the policy covers the vehicles only while actually engaged in hauling. That contention was considered and repudiated

by this court in a unanimous decision in the Mitchell case, supra. * * *

“Applying the legal principle announced in the Mitchell case to the situation here presented, to wit, that the collision and damage occurred while the tractor, after being repaired, was being driven to a place to get the trailer and thence to the plant of Glenn Cartage to resume hauling for it, the conclusion is inescapable that during any or all parts of that operation the equipment was within the coverage of the policy. That is unmistakably true unless we were willing to recede from the position established by the Mitchell case. In the instant case the movement was in the transportation service within the meaning of the policy, although such vehicle was not then being operated for the transportation of freight.”

(Pages 84-85.)

See also:

Mitchell v. Great Eastern Stages, Inc., 140 Ohio St. 137, 42 N.E. (2d) 771.

IV.

THE TRIAL COURT DID NOT COMMIT ERROR IN DENYING THE DEFENDANT'S MOTIONS.

In its title VII on page 27 of its brief, defendant contends that the trial court committed error in denying certain motions. We will answer these contentions in the order presented.

- (a) **The denial of defendant's motion for dismissal at the conclusion of plaintiffs' case was not error.**

This contention is in effect merely a reiteration of the contention made by defendant that the burden of proving the exception in the declaration was upon plaintiffs, and has been fully covered elsewhere in this brief. In any event, if the denial of this motion was error, it was not prejudicial error. (*Parra v. Cleaver*, supra; *Peters v. Southern Pacific Co.*, supra; *Huston v. Schohr*, supra.)

- (b) **The denial of defendant's motion to set aside the order striking the plea of res adjudicata was not error.**

Under this title the defendant advocates the adoption by this court of an anomalous rule. The plaintiffs commenced their action for damages against Warner and Woodrow in the state court on August 8, 1946, these persons were defended by attorneys hired by the defendant, and judgment was recovered in favor of plaintiffs on September 16, 1947. (Tr. p. 5.) The answer shows that during the pendency of the state court action and on October 18, 1946, defendant filed a complaint for declaratory relief in the Federal court against its insured, Warner and Woodrow, and against these plaintiffs. (Tr. pp. 13-14.)

In that action the defendant's insured were being sued by the same attorneys who were at the same time defending them in the pending state court action (Tr. pp. 15, 171). The defendant took judgment against Warner by default on August 14, 1947 (Tr. p. 15). In the state court action the plaintiffs herein recovered

judgment against Warner and Woodrow on September 16, 1947 (Tr. p. 5). On October 27, 1947, the defendant obtained a default judgment against its insured, Woodrow (Tr. p. 17).

It is not alleged nor contended that either of the plaintiffs herein was subject to the jurisdiction of the Federal court or served with process or that either appeared in the declaratory relief action therein. The defendant, nevertheless, contends that these plaintiffs are bound by the judgment. The facts concerning this action for declaratory judgment and the law applicable thereto are discussed by Judge Yankwich in the notes to the text of his opinion (Tr. pp. 67-68).

There may be added, however, reference to Rule 19 (b) of the Federal Rules of Civil Procedure.

“(b) *Effect of Failure to Join.* When persons who are not indispensable, but who ought to be parties if complete relief is to be accorded between those already parties, have not been made parties and are subject to the jurisdiction of the court as to both service of process and venue and can be made parties without depriving the court of jurisdiction of the parties before it, the court shall order them summoned to appear in the action. The court in its discretion may proceed in the action without making such persons parties, if its jurisdiction over them as to either service of process or venue can be acquired only by their consent or voluntary appearance or if, though they are subject to its jurisdiction, their joinder would deprive the court of jurisdiction of the parties before it; *but the judgment rendered*

therein does not affect the rights or liabilities of absent persons." (Italics added.)

In Restatement of the Law of Judgments, Section 79, page 357, the rule is thus stated:

"If a person is named as a party to the action but he is neither named nor otherwise described in the judgment, he is not a party to the judgment and is not affected by the decision of issues leading to it. * * * Conversely, if a person is not served and jurisdiction over him is not otherwise acquired and he does not appear or intervene in the action, the judgment is void as to him although his name appears therein."

The defendant calls attention to a letter sent to Warner and Woodrow by the writer as attorney for plaintiffs in the state court action, the sole purpose of which was to prevail upon Warner and Woodrow to defend the action for declaratory relief so as to avoid the possibility of the contention that the defendant now makes. The conduct of the defendant and its attorneys in suing its insured and clients while at the same time defending them in another action can best be described by references to the language used by the Supreme Court of Vermont in *Beatty v. Employers' Liability Assur. Corp.*, 106 Vt. 65, 168 A. 919.

"That no man can serve two masters is as true today as it was when the words were first spoken. A lawyer, retained by an insurance company to defend a case on behalf of a policy holder, as long as he remains in the case, owes his complete and

entire fidelity to the person whom he represents. He cannot substitute the interests of the insurer for those of the insured, and the company that employs him cannot be heard to claim that the insured is not prejudiced when he pursues so reprehensible a course of conduct."

See also:

O'Morrow v. Borad, 27 Cal. (2d) 794, 798, 167 P. (2d) 483.

The fact that the writer, as attorney for the plaintiffs in the state court action, had knowledge of the pendency of the action for declaratory relief does not bind the plaintiffs in this action.

"A person is a stranger, even though he has knowledge of the suit, if, although he has a right to intervene therein, he is under no obligation to do so, and he does not by actual intervention bring himself within its binding effect."

50 C. J. S. 384.

(c) **The denial of defendant's motion for a new trial conditioned on a reversal is not error.**

This contention merits no reply, as it is elementary that the granting or refusing of a new trial is a matter resting in the sound discretion of the district judge, whose action in such respect is not reviewable for errors of fact except in the most exceptional circumstances. (*Aetna Casualty & Surety Co. v. Yeatts*, 122 F. (2d) 350; *Youdan v. Majestic Hotel Management Corp.*, 125 F. (2d) 15.)

CONCLUSION.

It is respectfully submitted that the judgment notwithstanding the verdict be reversed, with directions to the trial court to enter judgment on the verdict of the jury.

Dated, Berkeley, California,
February 25, 1949.

Respectfully submitted,
NATHAN G. GRAY,
Attorney for Appellants.

No. 12,056

IN THE
United States Court of Appeals
For the Ninth Circuit

GEORGE W. BOULTER and MARGRETTA
L. BOULTER,

Appellants,

vs.

COMMERCIAL STANDARD INSURANCE
COMPANY, a corporation,

Appellee.

APPELLEE'S PETITION FOR A REHEARING.

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L. BOULTER,
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Appellants,

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APPELLEE'S PETITION FOR A REHEARING.

*To the Honorable William Denman, Presiding Judge,
and to the Honorable Associate Judges of the
United States Court of Appeals for the Ninth
Circuit:*

Appellee herewith petitions this Honorable Court to grant a rehearing in the above-entitled matter to the end that errors which appear in the Opinion may be corrected and the judgment of the trial Court reinstated, or, in the alternative, the controversy be remanded to the trial Court with instructions to reconsider Appellee's Motion for New Trial in the light of all the evidence.

The grounds upon which Appellee requests such rehearing are as follows:

I. The assumption of the fact (made by this Court) that Warner was “merely cruising in search of loads” at the time the accident happened is contrary to the uncontradicted and unimpeached evidence in the record.

II. The suggestion in the Opinion that the use to which the vehicle was being put at the time of the accident was a use covered by the insurance policy in question is contrary to law.

III. This Court, if it adheres to the conclusion (expressed in its Opinion) that there was evidence that, at the time of the accident, Warner was “merely cruising in search of loads”, erred in failing to remand the controversy to the trial Court with directions to reconsider Appellee’s alternative Motion for New Trial in the light of such evidence (which this Court now holds existed, but the existence of which we deny), since the trial Court (by ignoring the possible existence of such evidence) failed in its duty to exercise discretion in passing on the weight and sufficiency of any such evidence.

ARGUMENT.

I. THE ASSUMPTION OF THE FACT (MADE BY THIS COURT) THAT WARNER WAS "MERELY CRUISING IN SEARCH OF LOADS" AT THE TIME THE ACCIDENT HAPPENED IS CONTRARY TO THE UNCONTRADICTED AND UNIMPEACHED EVIDENCE IN THE RECORD.

It is respectfully submitted that in the opinion of this Court, published June 27, 1949, by which judgment in favor of the Appellee was reversed and judgment ordered entered in favor of Appellants, this Court has made assumptions of fact which are flatly contrary to the uncontradicted and unimpeached evidence which was before the jury and the trial judge when he directed a verdict in favor of Appellee.

The opinion of this Court, as we read it, is based on the assumption that, at the time the accident happened, Warner, the assured, was southbound from Eureka to San Francisco, with the dual purpose of (i) paying a premium on his insurance policy and (ii) then proceeding on to San Jose with the intention of soliciting Dowdell for a hauling job *to be performed at that time and before the assured returned to the Eureka area for his trailer, i.e. that he was "merely cruising in search of loads."*

This assumption, we submit, is erroneous, because the evidence lends itself to no other conclusion than that at the time of the accident Warner was bound for San Francisco *with the unqualified intention of returning to Eureka before engaging in any hauling operations for Dowdell, or anyone else.*

The most that can be said for Warner's intentions with respect to Dowdell is (we submit) that he intended merely to get in touch with Dowdell concerning the possibility of a future hauling job, but there is no evidence whatsoever that Warner intended to haul for Dowdell or anyone else before returning to Eureka to pick up his trailer. The evidence, indeed, is to the contrary.

It is the position of this Court (as we read the opinion) that, at the moment of the accident, Warner was a wildcat operator "merely cruising in search of loads", or "in anticipation of procuring a load", and that any intention he had with respect to the payment of a premium on his insurance policy merely made his trip a "dual purpose" trip which combined operations covered by the policy with operations not covered by the policy.

We can see no basis on which this Court can ignore the uncontradicted testimony which Warner gave in the State Court action, and which was before the jury in this case, and before Judge Yankwich when he directed a verdict in favor of the Appellee. This testimony reads (in part) as follows (Tr. 153):

"Q. At the time of this accident, you were returning to San Francisco?

A. That's right.

Q. You were returning back to continue with your business?

A. No, I had a definite purpose in coming down, I might state. I had a payment due on my insurance policy Monday. My policy would

lapse if I did not get in here Monday. That was the reason for coming down [to] Frisco, here.

Q. So you came down for that business?

A. That's right.

Q. *And when did you intend to return for your tractor?*

A. *The following day.*

Q. *For your trailer?*

A. *The following day."*

(Counsel had inadvertently said "tractor" when he meant "trailer". See Tr. 153.)

In the numerous cases cited by us (Appellee's Brief pp. 13-21) and referred to by this Court in its opinion (Footnote No. 3) the assured had, prior to or immediately subsequent to the accident in question, been engaged in operations which were clearly covered by the policy, but in none of the cases was the general intent to engage in an operation covered by the policy considered any basis for extending coverage to a specific operation where the intent was demonstrably otherwise and the operation, therefore, not covered by the policy. *Smith v. Calif. Highway Indem. Exchange*, 218 Cal.325; 23 Pac.(2d) 274 (referred to in the Opinion), presents no different rule: in that case the Court held that the assured was actually engaged in an operation "incidental" to his taxi-cab business when the accident happened.

There is no evidence, we respectfully submit, on which this Court can predicate its conclusion that, at the time of the accident, Warner intended to continue

on from San Francisco to San Jose for the purpose of soliciting and *then and there* engaging in carrying merchandise before returning to Eureka to pick up his trailer, *even if the opportunity had arisen*.

Warner testified that it had been his intention to carry a load from Eureka back to San Francisco (Tr. 107); and there is no evidence that he ever departed from this intention, which he in fact carried out.

He was interrogated respecting his intention in making the trip on which the accident occurred. He testified (Tr. 110-111):

“Q. Now what was your purpose in going to San Francisco?

A. There was an installment due on the policy, this policy. It was due on a Monday morning, or it was due, anyway—I forget how many hours I had grace, but that was my reason for coming to San Francisco as I did, without the trailer.

Q. And did you arrive in San Francisco?

A. I did.

Q. Did you make the run from Eureka to San Francisco without the trailer?

A. I did.

Q. And did this accident happen on that run?

A. Yes.”

He further testified (Tr. 114-115):

“Q. Now this accident happened on your way to San Francisco, is that correct?

A. That’s right.

Q. And after the accident you continued on to San Francisco, is that correct?

A. That’s correct.

Q. And how many days did you stay in San Francisco?

A. I was in until, I went down to the insurance company and notified the insurance company on Monday morning of the accident, and I paid my premium. That was on a Monday morning. Tuesday morning—Wednesday morning I left for Eureka, back up again. I had had the truck repaired Monday, the tractor rather, here in town. I went back up again to get my trailer.”

He was then interrogated by the Court respecting his *subsequent* return to San Francisco, after he had returned to Eureka and picked up his trailer, in accordance with his avowed intention. He testified (Tr. 115-116):

“A. Then I came back to San Francisco.

The Court. Q. Well did you pick up your trailer? And [were] the pipes then unloaded from your trailer?

A. Everything had been unloaded. I had a haul at the time with John Dowdell, of San Jose. That is John Dowdell, Draymen; I believe we were hauling concrete pipe out of San Jose for housing projects all over the area, the peninsula area. That was one of the——

Q. Well the point is this; you came back empty?

A. Yes.

Q. You just went back to get the trailer?

A. No, I got my trailer, and——

Q. By the way, when you came back the first time, when you came to San Francisco, was your wife with you?

A. My wife was with me.

Q. When did she come back—was she with you at the time of the accident?

A. She was with me at the time of the accident.

Q. Well did you leave her behind when you went back again?

A. Yes I did.

Q. You went back alone?

A. Yes.

Q. And you went back to get the trailer?

A. That's right.

Q. And the only reason you came back to San Francisco instead of waiting until the pipe was unloaded was because you wanted to return back and pay this premium?

A. To pay my premium, yes sir.

Q. I see."

Warner's proposed activities for Dowdell in the San Jose area were (as the testimony just quoted discloses) manifestly connected with a point in time which occurred *after* he had returned to Eureka to pick up his trailer. Thus, in speaking of his eventual return to San Francisco after he had picked up his trailer, he stated (Tr. 120-121):

"Q. Then when did you come back again?

A. Thursday morning.

Q. The very next Thursday morning or a week later?

A. No, that same Thursday morning.

Q. I see. And was your trailer loaded as you made that trip south?

A. Well I had a big range and some other stuff coming back home.

Q. Who owned that range?

A. It belonged to my sister too. I got \$64 bringing it back.

Q. And where did you deliver that?

A. I delivered that, to, I believe, my mother's place, at Number 10 Ord Court.

Q. *I see. Then was it after that that this San Jose contract came up that you were telling us about?*

A. *That's right, the following morning, I believe that was a Friday morning. I left for Carmel.*

Q. *Yes. I see. Now did you get that contract after you got back to San Francisco?*

A. *I did."*

Even under prompting by counsel for the Appellants Warner at no time claimed that it was his intention, if Dowdell offered him a hauling job, to haul for Dowdell (or anyone else) before returning to Eureka. He merely said that it was his intention "to talk to him [Dowdell] about hauling merchandise" (Tr. 128) and "to discuss with someone in San Jose the hauling of a load" (Tr. 127). Indeed, from all that appears in the record, he might have intended to talk to Dowdell or someone else about some hauling job in the past.

In an effort to make it appear that Warner had hoped or intended immediately to haul for Dowdell before again returning to the Eureka area, counsel for the Appellants (Tr. 140) asked Warner if the fact

that his vehicle was tied up for repairs in San Francisco was the reason "why you did not communicate with Dowdell". Even under this prompting Warner did not claim that he had intended at that time and before returning to Eureka to engage in a haul for Dowdell even if one were offered. He merely answered, "Well, I guess that would be as good a reason as any".

Warner did not claim that that was *his* reason and his "guess" can hardly be made the basis (we submit) for overturning the ruling of the trial Court directing a verdict for the Appellee. See *Galloway v. U. S.* (1943), 319 U.S. 372; *Connelly v. U. S.*, C.C.A. 5 (1941), 123 Fed. (2d) 1, and *Alexander v. Standard Accident Insurance Company*, C.C.A. 10 (1941), 122 Fed. (2d) 995, from which we quote at pages 24 and 25 of our brief, and in which the Courts sustained judgments on directed verdicts with the statement (in effect) that such judgments would not be overturned for "mere speculation", or where the record presented a "mere choice of probabilities".

Quite apart from that, Warner's "guess" merely referred to his plan to "communicate" with Dowdell; it did not refer to an intention to haul before returning to Eureka.

It is true, of course, that Dowdell *might* have had work for Warner had Warner solicited him when he arrived in San Francisco. However, again, there is no evidence whatsoever that Warner intended to accept such work. Indeed, as we have shown, the only

evidence is to the contrary, and even though the accident had not happened, we submit that the record lends itself to no other construction than that Warner intended to return to Eureka and get his trailer before engaging in any further hauling operations for Dowdell or anyone else.

That Warner's intentions with respect to performing any hauling job he might obtain from Dowdell were directed to a point in time which would occur *after* he had returned to Eureka, picked up his trailer, and again returned to the San Francisco area, is also clear from the following testimony (Tr. 166):

“Q. And you intended, after bringing your tractor and the trailer back to San Francisco, to go to San Jose and see if Mr. Dowdell had some hauling you could do for him, is that right?

A. Yes.”

II. THE SUGGESTION IN THE OPINION THAT THE USE TO WHICH THE VEHICLE WAS BEING PUT AT THE TIME OF THE ACCIDENT WAS A USE COVERED BY THE INSURANCE POLICY IN QUESTION IS CONTRARY TO LAW.

We note that this Court states in its opinion that “even if the errand to pay the premium was an excluded use, which we are not prepared to say, the only consequence would be that Warner combined a purpose to procure hauling with a purpose to pay a ‘bill’”, and that if the trip is to be construed as “a multiple purpose trip, in part for non-transportation purposes”, coverage extended at the time of the accident.

If this Court is of the opinion that Warner was using the vehicle in this instance for driving from

Eureka to San Francisco for the sole purpose of paying the premium on an insurance policy and that that was a covered use, we submit that the opinion runs counter to established law as evidenced in the numerous cases above referred to (Opinion, footnote No. 3 and Appellee's Brief pp. 13-21). An added intention (if it existed) to communicate with Dowdell about hauling operations to take place *after Warner had returned to Eureka, picked up his trailer, and once again headed south* involves a mere *general commercial use* of the vehicle, and is not a necessary incident of the business of transportation of merchandise, as the same cases indicate, and is, accordingly, a non-covered use.

Liability insurance coverage for general commercial purposes was available and Warner could have purchased it had he so desired. He undertook to use his vehicle for general commercial purposes without procuring and paying for such coverage and he was using his vehicle for such non-covered purposes at the time the accident happened.

This Court has, in its opinion, given Warner the benefit of a bargain he did not make, and, by the same token, has given the Appellants the benefit of a bargain which was not made.

That Appellee's policy contained no restriction on the "manner in which the 'transportation of merchandise' business is to be conducted" (as this Court pointed out in the opinion) does not, we submit, permit the conclusion that a "wildcat operator", every time he drives his vehicle on the highway, is engaged

in the "transportation of merchandise" or in an activity "for which authorization is required" by the California Highway Carrier Act when, as to the specific occasion involved, the evidence is that he was engaging in an operation which involved a mere commercial use of the vehicle only remotely connected with the "covered" use.

That a purely "incidental" use of a vehicle must be far more immediate to a covered use than the use here involved, in order to avail the user of the benefits of a policy by its terms limited to a specific use, is established, we submit, by the cases referred to in our brief (Appellee's Br. pp. 13-21) and the Opinion of this Court (Footnote 3).

III. THIS COURT, IF IT ADHERES TO THE CONCLUSION (EXPRESSED IN ITS OPINION) THAT THERE WAS EVIDENCE THAT, AT THE TIME OF THE ACCIDENT, WARNER WAS "MERELY CRUISING IN SEARCH OF LOADS", ERRED IN FAILING TO REMAND THE CONTROVERSY TO THE TRIAL COURT WITH DIRECTIONS TO RECONSIDER APPELLEE'S ALTERNATIVE MOTION FOR NEW TRIAL IN THE LIGHT OF SUCH EVIDENCE (WHICH THIS COURT NOW HOLDS EXISTED, BUT THE EXISTENCE OF WHICH WE DENY), SINCE THE TRIAL COURT (BY IGNORING THE POSSIBLE EXISTENCE OF SUCH EVIDENCE) FAILED IN ITS DUTY TO EXERCISE DISCRETION IN PASSING ON THE WEIGHT AND SUFFICIENCY OF ANY SUCH EVIDENCE.

It is well established that the refusal of a trial Court to exercise discretion in passing upon the weight and sufficiency of the evidence on a Motion for a New Trial is reversible error. *Southern Pacific Co. v. Klinge*, C.C.A. 10 (1933), 65 Fed. (2d) 85; 11 Cyclo-

pedia of Federal Procedure (2nd Edition) section 6036.

It was obviously the duty of the trial judge, in passing on our alternative Motion for a New Trial, to consider *all* of the evidence before him. If he, sitting as a "13th juror", felt that the evidence was not satisfactory, it was his duty, of course, to grant a new trial in accordance with our Motion, and in arriving at a determination as to the weight and sufficiency of the evidence it was his duty to consider *all* of the evidence.

It is patent from Judge Yankwich's Opinion* that he adhered to the view that the evidence showed only that, at the time the accident happened, Warner was bound for San Francisco with the intention of (i) paying a premium on his insurance policy and (ii) the unresolved intention of soliciting business from Dowdell. There is no suggestion in the Opinion that Judge Yankwich held the view that Warner was "merely cruising in search of loads" or that he intended to haul for Dowdell before completing the "non-covered" use and returning to Eureka to pick up his trailer

*Whether the trial court exercised any discretion in passing on the weight and sufficiency of the evidence on our Motion for New Trial may, of course, be ascertained from its Opinion. *Coakley v. Ajuria* (1930), 209 Cal. 745 at 749, 290 Pac. 33:

"We think the learned trial judge took an erroneous view of the law applicable to the facts, as is made apparent from an oral opinion which he delivered * * *. While the reasons of a trial court so given do not in a strict sense constitute a part of the record on appeal, yet where they furnish, as in this case, the basis of the court's action, and really constitute the only grounds upon which the judgment may be affirmed, it is proper to give them special consideration. * * *" (209 Cal. 745 at 749.)

even had his (claimed) intent to solicit from Dowdell resulted in a hauling operation.

Judge Yankwich, in short, wholly failed to consider the weight and sufficiency of evidence (which this Court now holds existed) from which (as this Court feels) it could have been determined that Warner was “merely cruising in search of loads”. If the evidence on this point had not been satisfactory to Judge Yankwich, he might well, in the exercise of his discretion, have granted a new trial. In any event, we were entitled to have him exercise his discretion and pass upon the weight and sufficiency of such evidence, and it is clear from his opinion that he did not do so, since he patently did not feel that any such evidence existed.

By way of illustration we restate this principle as follows:

In passing upon our Motion for New Trial, Judge Yankwich assumed, from the evidence, the existence of only facts A and B; he held that, *as a matter of law*, the existence of facts A and B would not sustain the verdict of the jury. Accordingly, he granted judgment notwithstanding the verdict, but stated (in effect) that if he was wrong on the point of law, and that if facts A and B *were* sufficient to sustain the verdict, there was no occasion for granting a new trial, as the evidence was legally sufficient to establish the existence of facts A and B.

He did not consider whether there was any evidence of fact C, (“merely cruising in search of loads”), and,

accordingly, did not exercise his duty of sitting as a "13th juror" in passing on the weight and sufficiency of any evidence claimed to support the existence of fact C.

Again, this Court has now held (as we read the Opinion) that there was evidence of fact C. Judge Yankwich (as his Opinion demonstrates) exercised no discretion in passing upon the weight and sufficiency of the evidence in support of fact C, because he never considered its existence or non-existence. We were entitled to have him exercise discretion in passing on that point, and his failure to do so was reversible error under the rule of *Southern Pacific Co. v. Klinge*, supra.

We are not unmindful of the rule that new points will not "ordinarily" be considered for the first time on a petition for rehearing. However, in this instance we appeal to the discretionary powers of this Court over its own procedure in view of the fact that this Court's Opinion contains the first suggestion in this litigation, by either Court or counsel, that Warner was "merely cruising in search of loads" at the time the accident happened.

In these circumstances we respectfully request that this Court, if it declines to reinstate Judge Yankwich's Order granting judgment notwithstanding the verdict, remand the controversy to Judge Yankwich with directions to exercise discretion in passing upon the weight and sufficiency of the evidence on our motion for new trial in the light of the existence of *all* the evidence which this Court now holds is contained in the record.

Stated another way, Judge Yankwich should be required to pass upon the weight and sufficiency of any evidence claimed to support the factual assumption of this Court that Warner was merely "cruising in search of loads" at the time of the accident.

IV. CONCLUSION.

It is respectfully submitted that a rehearing should be granted to the end that the judgment of the trial Court be reinstated or, in the alternative, that the controversy be remanded to the trial Court with directions to reconsider our motion for new trial in the light of all the evidence.

Dated, San Francisco, California,

July 27, 1949.

Respectfully submitted,

PAUL C. DANA,

LEIGHTON M. BLEDSOE,

ROGERS P. SMITH,

R. S. CATHCART, and

DANA, BLEDSOE & SMITH,

*Attorneys for Appellee
and Petitioner.*

R. S. CATHCART,

Of Counsel.

CERTIFICATE OF COUNSEL.

I hereby certify that I am of counsel for appellee and petitioner in the above entitled cause and that in my judgment the foregoing petition for a rehearing is well founded in point of law as well as in fact and that said petition for a rehearing is not interposed for delay.

Dated, San Francisco, California,
July 27, 1949.

R. S. CATHCART,
*Of Counsel for Appellee
and Petitioner.*



No. 12057

United States
Court of Appeals
for the Ninth Circuit

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Appellant,

vs.

MATSON NAVIGATION COMPANY,
a corporation,
Appellee.

Transcript of Record

Appeal from the District Court of the United States
for the Northern District of California
Southern Division

NOV 1 - 1948

PAUL P. O'BRIEN,

No. 12057

United States
Court of Appeals

for the Ninth Circuit

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Appellant,

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MATSON NAVIGATION COMPANY,
a corporation,

Appellee.

Transcript of Record

Appeal from the District Court of the United States
for the Northern District of California,
Southern Division

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San Francisco, California,

Attorneys for Defendant and Appellant.

BRODECK, PHLEGER and HARRISON,

111 Sutter Street,
San Francisco, California,

Attorneys for Plaintiff and Appellee.

In the District Court of the United States for the
Northern District of California,
Southern Division

No. 27856-G

MATSON NAVIGATION COMPANY,
Plaintiff,

vs.

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Defendant.

**ACTION FOR DAMAGES FOR BREACH OF
CONTRACT UNDER THE LABOR MAN-
AGEMENT RELATIONS ACT OF 1947.**

The action arises under the Labor Management Relations Act of 1947, Chapter 120, Public Law 101, Title III, Section 301, hereinafter referred to as 'the Act'. Matson Navigation Company, a corporation, for cause of action against National Union of Marine Cooks and Stewards, an unincorporated association, alleges:

I.

Matson Navigation Company, plaintiff herein, was at all times mentioned in this complaint, and now is, a corporation duly organized and existing under and by virtue of the laws of the State of California, and doing business therein.

Plaintiff is and at all times herein mentioned has been the owner and operator of the vessel SS. Hawaiian Craftsman. [1*]

* Page numbering appearing at foot of page of original certified Transcript of Record.

II.

National Union of Marine Cooks and Stewards, defendant herein, is and at all time mentioned herein has been an unincorporated association composed of employees performing work in the Stewards' Department of vessels, including those operated by plaintiff, sailing out of Pacific Coast ports of the United States to other American ports and ports of foreign countries upon the high seas and upon navigable waters of the United States. Defendant is and at all times herein mentioned has been a labor union or labor organization with its principal office and place of business in the City and County of San Francisco in the Northern District of California, and is and at all times herein mentioned has been engaged in its business and activities as a labor union or organization in the City and County of San Francisco in the Northern District of California. Defendant is hereinafter sometimes referred to as the "Union". Defendant at all times herein mentioned represented members of the Stewards' Department of the SS Hawaiian Craftsman as a labor organization and collective bargaining agent in accordance with the provisions of the agreement hereinafter set forth.

III.

On or about November 26, 1946, plaintiff and defendant made and entered into a certain contract providing for and fixing, among other things, the wages, hours, working conditions and other conditions of employment of the personnel employed by plaintiff in the Stewards' Department of ves-

sels operated by plaintiff, including the vessel SS Hawaiian Craftsman. Said contract is one of maritime services, and was entered into between plaintiff, as employer, and defendant, which is [2] a labor organization representing employees in the shipping industry, an industry affecting commerce as defined in the Act. A true and correct copy of said contract is attached hereto as Exhibit A and made a part hereof by reference. Said contract and the provisions thereof were in full force and effect at all times mentioned herein.

IV.

In and by said contract the plaintiff agrees "to give preference in employment to members of the Union and to secure employees in their Stewards' Department through the offices of the Union", and the defendant agrees "to furnish capable, competent and satisfactory employees" to plaintiff. Said contract further provides that there "shall be no strikes, lockouts or stoppages of work while the provisions of this agreement are in effect."

V.

On December 30, 1947, on or about 9:00 a.m., said steamship Hawaiian Craftsman was lying in the navigable waters of the United States in the port of Tacoma, Washington, and was being prepared and made ready for a voyage shortly to commence from said port to the port of Portland, Oregon. At said time and place plaintiff submitted to the employees in the Stewards' Department of said vessel for signature, and requested that they sign, shipping articles in the customary form for said voyage, but defendant instructed, and had in-

structed, the said employees in the Stewards' Department of said vessel to refuse to sign said shipping articles until and unless plaintiff should agree to pay to certain of said Stewards' Department crew members certain overtime pay for a previous voyage of said vessel. Pursuant to said instructions given them by defendant, as [3] aforesaid, and in violation of the said contract, the crew members of the Stewards' Department of said vessel refused to sign said shipping articles and to sail said vessel. Defendant from December 30, 1947, as aforesaid, to 6:17 p.m. January 10, 1948, violated its contract by engaging in a strike and stoppage of work against plaintiff during said period and by failing and refusing to furnish Stewards' Department employees to plaintiff as required by the said contract.

VI.

At all times herein mentioned defendant maintained at Seattle, Washington, an office or hiring hall for the purpose of furnishing and dispatching Stewards' Department crew members to vessels in the Puget Sound area, including vessels at the port of Tacoma, Washington. From time to time during the period from December 29, 1947 to January 10, 1948, inclusive, plaintiff requested defendant, in accordance with said contract, by orders placed with said office or hiring hall and otherwise, to furnish Stewards' Department employees to man and sail said vessel, but defendant, in violation of said contract, failed and refused to furnish plaintiff with said employees as aforesaid.

VII.

Said vessel completed loading at Tacoma, Wash-

ington on or before 6:00 p.m. of January 2, 1948, and was then and there ready and scheduled to depart. Because of the failure and refusal of defendant to man and sail said vessel, and because of defendant's strike and stoppage of work, said vessel was prevented by defendant from departing from said port until 6:17 p.m. January 10, 1948. As a direct and proximate result of [4] said failure and refusal of defendant to man said vessel and the strike and stoppage of work by defendant resulting in the delay and detention of said vessel as aforesaid, all in violation of said contract, plaintiff has been damaged in the amount of \$17,000.

VIII.

Plaintiff has at all times performed all conditions precedent provided or required by the contract herein referred to and has performed each and all of the obligations under said contract.

Wherefore, plaintiff demands judgment in the sum of \$17,000, with interest thereon at the legal rate from January 15, 1948, to the date of payment, and the costs of this action.

BROBECK, PHLEGER &
HARRISON,

/s/ MARION B. PLANT,
Attorneys for Plaintiff.

(Here follows agreement between National Union of Marine Cooks and Stewards and Pacific American Shipowners Association dated: November 26, 1946—Exhibit A.)

[Endorsed]: Filed Jan. 15, 1948. [5]

[Title of District Court and Cause.]

MOTION FOR STAY OF PROCEEDINGS

Comes now the defendant above named and, for the reasons and upon the grounds hereinafter set forth, moves the above entitled Court for its order staying proceedings herein pursuant to Section 3 of the Federal Arbitration Act (9 U.S.C.A. § 3).

Said motion is made upon the grounds that it appears from the face of the complaint on file herein, and the exhibit attached thereto, that one or more issues are presented which are referable to arbitration under a written collective bargaining agreement.

Said motion is based upon the said written collective bargaining agreement, a copy of which is attached to said complaint as an exhibit, and upon a Memorandum of Points and Authorities herewith submitted.

Said motion is further based upon the fact, which said defendant hereby asserts to be true, that the said defendant (applicant in this motion) is not in default in proceeding with said arbitration under said collective agreement. [6]

Dated: This 8th day of April, 1948.

**GLADSTEIN, ANDERSEN,
RESNER & SAWYER,**

**By RICHARD GLADSTEIN,
Attorneys for Defendant.**

**Memorandum of Points and Authorities
9 U.S.C.A. § 3**

Agostine Bros. Building Corp. vs. U.S., 142
Fed. (2d) 854 (4th Circuit)

Gerald Donahue vs. Susequehana Collieries
Co., 138 Fed. (2d) 3 (3rd Circuit)

Shanferoque Coal & Supply Co. vs. Westchester Service Co., 70 Fed. (2d) 297 (2nd Circuit)

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed Apr. 8, 1948. [7]

In the United States District Court, for the Northern District of California, Southern Division

No. 27856-G

MATSON NAVIGATION COMPANY,

vs. Plaintiff,

NATIONAL UNION OF MARINE COOKS

AND STEWARDS, ETC., Defendant.

ORDER DENYING MOTION TO STAY PROCEEDINGS PENDING ARBITRATION

The Federal Arbitration Act of February 12, 1923 (9 USC § 1 et seq.) is not applicable to actions maintained, as in this cause, pursuant to § 301 of the National Labor Management Relations Act of 1947, Pub. Law 101, 80th Cong. C. 120. Colonial Hardwood Flooring Co. v. International Union United Furniture Workers of America, et al. 76 Fed. Supp. 493.

The action to stay proceedings is denied.

Dated: May 12, 1948.

LOUIS E. GOODMAN,

United States District Judge.

[Endorsed]: Filed May 12, 1948. [8]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that National Union of Marine Cooks and Stewards, an unincorporated association, defendant above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the order of the above entitled court denying motion to stay proceedings pending arbitration, entered in this action on the 12th day of May, 1948.

Dated this 25th day of May, 1948.

GLADSTEIN, ANDERSEN,
RESNER & SAWYER,
/s/ RICHARD GLADSTEIN,

By /s/ NORMAN LEONARD,
Attorneys for Defendant.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 9, 1948. [9]

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

Comes now National Union of Marine Cooks and Stewards, an unincorporated association, defendant and appellant herein and designates the following as the record on appeal in the above entitled matter:

1. Complaint for damages, for breach of contract under the Labor-Management Relations Act

of 1947, filed herein on January 15, 1948, and Sections 1, 2, 3, 4, 5, 6, 7, 8, 11, 12, 13, 15, 16, 17, 18 and 20 of Exhibit A attached to said complaint.

2. Motion for Stay of Proceedings filed herein on April 8, 1948.

3. Order Denying Motion to Stay Proceedings Pending Arbitration filed herein May 12, 1948.

4. Notice of Appeal filed herein June 9, 1948.

5. This Designation of Record on Appeal dated June 11th, 1948.

GLADSTEIN, ANDERSEN,
RESNER & SAWYER,

By /s/ RICHARD GLADSTEIN,

By /s/ NORMAN LEONARD,
Attorneys for Defendant.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 12, 1948.] [10]

[Title of District Court and Cause.]

DESIGNATION BY PLAINTIFF AND RE-
SPONDENT OF ADDITIONAL PORTIONS
OF RECORD ON APPEAL.

Plaintiff and respondent, Matson Navigation Company, hereby designates the following portions of the record in the above action in addition to those designated by defendant and appellant in its Designation of Record on Appeal on file herein:

1. All of Exhibit A attached to the Complaint on file herein.

2. This Designation by Plaintiff and Respondent of Additional Portions of Record on Appeal.

Dated: June 18, 1948.

BROBECK, PHLEGER &
HARRISON,

By ROBERT E. BURNS,
Attorneys for Plaintiff and
Respondent.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 18, 1948. [11]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET

Good cause appearing therefor, it is hereby ordered that the Appellant herein may have to and including August 28, 1948, to file the Record on Appeal in the United States Circuit Court of Appeals in and for the Ninth Circuit.

Dated: July 19, 1948.

DAL M. LEMMON,
United States District Judge.

[Endorsed]: Filed June 19, 1948. [12]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET

Good cause appearing therefor, it is hereby ordered that the Appellant herein may have to and including September 7, 1948, to file the Record on Appeal in the United States Circuit Court of Appeals in and for the Ninth Circuit.

Dated: August 26, 1948.

MICHAEL J. ROCHE,
United States District Judge.

[Endorsed]: Filed Aug. 26, 1948. [13]

District Court of the United States,
Northern District of California

CLERK'S CERTIFICATE

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 13 pages, numbered 1 to 13, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of Matson Navigation Company, Plaintiff, vs. National Union of Marine Cooks and Stewards, an unincorporated association, Defendant, No. 27856-G, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of \$4.50 and that the said amount

has been paid to me by the Attorney for the appellant herein.

In witness whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 7th day of September, A.D. 1948.

(Seal)

C. W. CALBREATH,
Clerk. [14]

[Endorsed]: No. 12057. United States Court of Appeals for the Ninth Circuit. National Union of Marine Cooks and Stewards, an unincorporated association, Appellant, vs. Matson Navigation Company, a corporation, Appellee. Transcript of Record. Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed October 7, 1948.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

No. 12058

United States
Court of Appeals
for the Ninth Circuit

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Appellant,

vs.

LUCKENBACH STEAMSHIP COMPANY,
a corporation,
Appellee.

Transcript of Record

Appeal from the District Court of the United States
for the Northern District of California,
Southern Division

FILED

NOV 1 - 1948

No. 12058

United States
Court of Appeals
for the Ninth Circuit

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Appellant,

vs.

LUCKENBACH STEAMSHIP COMPANY,
a corporation,
Appellee.

Transcript of Record

Appeal from the District Court of the United States
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111 Sutter Street,
San Francisco, California,

Attorneys for Plaintiff and Appellee.

In the District Court of the United States for the
Northern District of California,
Southern Division

No. 27862-G

LUCKENBACH STEAMSHIP COMPANY,
Plaintiff,

vs.

NATIONAL UNION OF MARINE COOKS AND
STEWARDS, an unincorporated association,
Defendant.

AMENDED COMPLAINT FOR DAMAGES
FOR BREACH OF CONTRACT UNDER
THE LABOR MANAGEMENT RELATIONS
ACT OF 1947.

The action arises under the Labor Management Relations Act of 1947, Chapter 120, Public Law 101, Title III, Section 301, hereinafter referred to as "the Act".

Plaintiff Luckenbach Steamship Company, a corporation, files this amended complaint pursuant to Rule 15 of the Federal Rules of Civil Procedure, and for a first cause of action against National Union of Marine Cooks and Stewards, an unincorporated association, alleges:

I.

Luckenbach Steamship Company, plaintiff herein, was at all times mentioned in this complaint, and now is, a corporation duly organized and existing under and by virtue of the laws of the State of Delaware.

II.

Plaintiff is and at all times herein mentioned has been the charterer and operator of the vessel SS Leonidas Polk. [1*]

III.

National Union of Marine Cooks and Stewards, defendant herein, is and at all times mentioned herein has been an unincorporated association composed of employees performing work in the Stewards' Department of vessels, including those operated by plaintiff, sailing out of Pacific Coast ports of the United States to other American ports and ports of foreign countries upon the high seas and upon navigable waters of the United States. Defendant is and at all times herein mentioned has been a labor union or labor organization with its principal office and place of business in the City and County of San Francisco in the Northern District of California, and is and at all times herein mentioned has been engaged in its business and activities as a labor union or organization in the City and County of San Francisco in the Northern District of California. Defendant is hereinafter sometimes referred to as the "Union".

IV.

Defendant at all times herein mentioned represented employees of plaintiff in the Stewards' Department of the said SS Leonidas Polk as a labor

* Page numbering appearing at foot of page of original certified Transcript of Record.

organization and collective bargaining agent in accordance with the provisions of the agreement hereinafter set forth.

V.

On or about November 26, 1946, plaintiff and defendant made and entered into a certain contract providing for and fixing, among other things, the wages, hours, working conditions and other conditions of employment of the personnel employed by plaintiff in the Stewards' Department of vessels operated by plaintiff, including the vessel SS Leonidas Polk. [2]

VI.

Said contract is one of Maritime service, and was entered into between plaintiff, as employer, and defendant, which is a labor organization representing employees in the shipping industry, an industry affecting commerce as defined in the Act. A true and correct copy of said contract is attached hereto as Exhibit A and made a part hereof by reference. Said contract and the provisions thereof were in full force and effect at all times mentioned herein.

VII.

In and by said contract the plaintiff agrees "to give preference in employment to members of the Union and to secure employees in their Stewards' Department through the offices of the Union", and the defendant agrees "to furnish capable, competent and satisfactory employees" to plaintiff. Said contract further provides that there "shall be no strikes, lockouts or stoppages of work while the provisions of this agreement are in effect".

VIII.

On February 25, 1947, said SS Leonidas Polk was lying in the navigable waters of the United States in the Port of Seattle, Washington, and was being prepared and made ready for a voyage shortly to commence from said Port of Seattle, Washington, to the Port of San Francisco, California. At said time and place plaintiff submitted to defendant an order for a complete complement of Stewards' Department employees for the above named vessel and voyage, to be on board not later than 9:00 a.m., February 26, 1947. Defendant failed and refused to furnish said employees, and at all times thereafter and until at or about 1:30 p.m., March 11, 1947, continued to fail and refuse to furnish said [3] employees. Defendant during said period from February 26, 1947, to 1:30 p.m. of March 11, 1947, engaged in a strike and stoppage of work against plaintiff, and thereby violated the said contract between the parties as more particularly hereinafter alleged.

IX.

At all times herein mentioned defendant maintained at Seattle, Washington, an office or hiring hall for the purpose of furnishing and dispatching Stewards' Department crew members to vessels in the Puget Sound area, including vessels at the Port of Seattle, Washington. From time to time during the period from February 26, 1947, to March 11, 1947, inclusive, plaintiff requested defendant, in accordance with said contract, by orders placed with said office or hiring hall and otherwise, to furnish Stewards' Department employees

to man and sail said vessel, but defendant, in violation of said contract, failed and refused to furnish plaintiff with said employees as aforesaid.

X.

Said vessel completed loading at Seattle, Washington, at or about 11:00 p.m. of March 5, 1947, and was then and there ready and scheduled to depart. Because of the failure and refusal of defendant to man and sail said vessel, and because of defendant's strike and stoppage of work, said vessel was prevented by defendant from departing from said port until 4:10 p.m., March 11, 1947. As a direct and proximate result of said failure and refusal of defendant to man said vessel, and the strike and stoppage of work by defendant resulting in the delay and detention of said vessel as aforesaid, plaintiff has been damaged in the amount of \$5,466.00 [4]

XI.

Plaintiff has at all times performed all conditions precedent provided or required by the contract herein referred to and has performed each and all of its obligations under said contract.

Luckenbach Steamship Company, a corporation, for a second cause of action against National Union of Marine Cooks and Stewards, an unincorporated association, arising under the Labor Management Relations Act of 1947, Chapter 120, Public Law 101, Title III, Section 301, hereinafter referred to as "the Act", alleges:

I.

Plaintiff refers to and incorporates herein, with the same force and effect as if herein set forth in

full, all the allegations contained in paragraphs I, III, VI, VII, and XI of its first cause of action.

II.

Plaintiff is and at all times herein mentioned has been the charterer and operator of the vessel SS Percy Foxworth.

III.

Defendant at all times herein mentioned represented employees in the Stewards' Department of the SS Percy Foxworth as a labor organization and collective bargaining agent in accordance with the provisions of the agreement herein set forth.

IV.

On or about November 26, 1946, plaintiff and defendant made and entered into a certain contract providing for and fixing, among other things, the wages, hours, working conditions and other conditions of employment of the [5] personnel employed by plaintiff in the Stewards' Department of vessels operated by plaintiff, including the vessel SS Percy Foxworth.

V.

On February 13, 1947, on or about 10:00 a.m., the SS Percy Foxworth was lying in the navigable waters of the United States in the Port of Seattle, Washington, and was being prepared and made ready for a voyage shortly to commence from said port to the Port of Yokohama, Japan. At said time and place plaintiff submitted to the employees in the Stewards' Department of said vessel for signature, and requested that they sign, shipping articles in the customary form for said voyage, but defendants instructed the said employees to

refuse to sign said shipping articles until and unless plaintiff should agree to change the articles in certain respects. Pursuant to said instructions given them by defendant, as aforesaid, and in violation of the said contract, the employees refused to sign said shipping articles and to sail said vessel. Defendant, from February 13, 1947, on or about 10:00 a.m., to February 19, 1947, violated its contract by engaging in a strike and stoppage of work against plaintiff during said period and by failing and refusing to furnish Stewards' Department employees to plaintiff as requested by the said contract.

VI.

On the forenoon of February 15, 1947, the SS Percy Foxworth was lying in the navigable waters of the United States in the Port of Seattle, Washington, and was being prepared and made ready for a voyage shortly to commence from said Port of Seattle, Washington, to the Port of Yokohama, Japan. At said time and place plaintiff submitted to defendant an order for a complement of Stewards' Department employees for the above named vessel and voyage, to replace [6] certain Stewards' Department employees then on board who refused to sign articles for said voyage, on instructions from defendant, and refused to man and sail said vessel, said replacements to be on board not later than midnight of February 15, 1947. Defendant failed and refused to furnish said employees, and at all times thereafter and until at or about 10:00 a.m., February 19, 1947, continued to fail and refuse to furnish said employees. Defendant during said period from February 15, 1947, to 10:00 a.m.

of February 19, 1947, engaged in a strike and stoppage of work against plaintiff and thereby violated the said contract between the parties as more particularly hereinafter alleged.

VII.

At all times herein mentioned defendant maintained at Seattle, Washington, an office or hiring hall for the purpose of furnishing and dispatching Stewards' Department crew members to vessels in the Puget Sound area, including vessels at Seattle, Washington. From time to time during the period from February 15, 1947, to February 19, 1947, inclusive, plaintiff requested defendant in accordance with said contract, by orders placed with said office or hiring hall and otherwise, to furnish Stewards' Department employees to man and sail said vessel, but defendant, in violation of said contract, failed and refused to furnish plaintiff with said employees as aforesaid.

VIII.

Said vessel completed loading at Seattle, Washington, at or about 10:00 p.m. of February 17, 1947, and was ready and scheduled to depart at 11:00 p.m. of said date. Because of the failure and refusal of defendant to man and sail said vessel, and because of defendant's strike and [7] stoppage of work, said vessel was prevented by defendant from departing from said port until 11:30 a.m., February 19, 1947. As a direct and proximate result of said failure and refusal of work by defendant, resulting in the delay and detention of said vessel as aforesaid, plaintiff has been damaged in the amount of \$1,456.00.

Luckenbach Steamship Company, a corporation, for a third cause of action against National Union of Marine Cooks and Stewards, an unincorporated association, arising under the Labor Management Relations Act of 1947, Chapter 120, Public Law 101, Title III, Section 301, hereinafter referred to as "the Act", alleges:

I.

Plaintiff refers to and incorporates herein with the same force and effect as if herein set forth in full all the allegations contained in paragraphs I, III, VI, VII, and XI of its first cause of action.

II.

Plaintiff is and at all times herein mentioned has been the charterer and operator of the vessel SS Douglas Victory.

III.

Defendant at all times herein mentioned represented employees in the Stewards' Department of the SS Douglas Victory as a labor organization and collective bargaining agent in accordance with the provisions of the agreement herein set forth.

IV.

On or about November 26, 1946, plaintiff and defendant made and entered into a certain contract providing for [8] and fixing, among other things, the wages, hours, working conditions and other conditions of employment of the personnel employed by plaintiff in the Stewards' Department of vessels operated by plaintiff, including the vessel SS Douglas Victory.

V.

On January 9, 1948, at or about 3:00 p.m., the

SS Douglas Victory was lying in the navigable water of the United States in the Port of Stockton, California, and was being prepared and made ready for a voyage shortly to commence from said port to the Port of San Pedro, California. At said time and place plaintiff submitted to the employees in the Stewards' Department of said vessel for signature, and requested that they sign, shipping articles in the customary form for said voyage, but defendant instructed the said employees to refuse to sign said shipping articles. Pursuant to said instructions given them by defendant, as aforesaid, and in violation of the said contract, the employees refused to sign said shipping articles and to man and sail said vessel. Defendant, from January 9, 1948. at or about 3:00 p.m., to January 13, 1948, at or about 1:00 p.m., violated its contract by engaging in a strike and stoppage of work against plaintiff during said period, and by failing and refusing to furnish Stewards' Department employees to plaintiff as requested by the said contract. During said period plaintiff requested said employees to sign said shipping articles on numerous occasions, but the said employees each and every time refused to sign same, until at or about 1:00 p.m., January 13, 1948, all pursuant to the instructions of defendant and by its direction. [9]

VI.

Said vessel completed loading at Stockton, California, on or before January 12, 1948, and was ready and scheduled to depart for the Port of San Pedro, California, in accordance with her sailing orders, at 8:45 a.m., January 12, 1948, at which

time, and solely because of the violation of said contract by defendant, as herein set forth, said vessel departed from Stockton, California, and put in the Port of San Francisco, California. Because of the failure and refusal of defendant to man and sail said vessel, and because of defendant's strike and stoppage of work, said vessel was prevented by defendant from departing from the latter port for the Port of San Pedro, California, until 3:00 p.m., January 13, 1948. As a direct and proximate result of the delay and detention of said vessel which resulted solely from the violation by defendant of its contract with plaintiff, as herein set forth, plaintiff has been damaged in the amount of \$2,092.00.

Wherefore, plaintiff demands judgment in the sum of \$9,014.00, with interest at the legal rate on \$5,466.00 from February 25, 1947, to date of payment; on \$1,456.00 from February 13, 1947, to date of payment; and on \$2,092.00 from January 9, 1947, to date of payment, together with costs of this action.

/s/ BROBECK, PHLEGER &
HARRISON,

/s/ MARION B. PLANT,
Attorneys for Plaintiff. [10]

(Acknowledgment of receipt of service.)

(Here follows Exhibit "A"—agreement between National Union of Marine Cooks and Stewards and Pacific American Shipowners Association dated: November 26, 1946.)

[Endorsed]: Filed Jan. 28, 1948. [11]

[Title of District Court and Cause.]

MOTION FOR STAY OF PROCEEDINGS

Comes now the defendant above named and, for the reasons and upon the grounds hereinafter set forth, moves the above entitled Court for its order staying proceedings herein pursuant to Section 3 of the Federal Arbitration Act (9 U.S.C.A. § 3).

Said motion is made upon the grounds that it appears from the face of the complaint on file herein, and the exhibit attached thereto, that one or more issues are presented which are referable to arbitration under a written collective bargaining agreement.

Said motion is based upon the said complaint, the said written collective bargaining agreement, a copy of which is attached to said complaint as an exhibit, and upon a Memorandum of Points and Authorities herewith submitted. [12]

Said motion is further based upon the fact, which said defendant hereby asserts to be true, that the said defendant (applicant in this motion) is not in default in proceeding with such arbitration under the said collective bargaining agreement.

Dated: This 2nd day of April, 1948.

**GLADSTEIN, ANDERSEN,
RESNER & SAWYER,
By RICHARD GLADSTEIN,
Attorneys for Defendant.**

Memorandum of Points and Authorities

9 U.S.C.A. § 3.

Agostine Bros. Building Corp. vs. U. S., 142
Fed. (2d) 854 (4th Circuit)

Gerald Donahue vs. Susquehanna Collieries Co., 138 Fed. (2d) 3 (3rd Circuit)

Shanferoque Coal & Supply Co. vs. Westchester Service Co., 70 Fed. (2nd) 297 (2nd Circuit)

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed Apr. 2, 1948. [13]

In the United States District Court, for the Northern District of California, Southern Division

No. 27862-G

LUCKENBACH STEAMSHIP COMPANY,
Plaintiff,

vs.

NATIONAL UNION OF MARINE COOKS
AND STEWARDS, and unincorporated association,
Defendant.

ORDER DENYING MOTION TO STAY PROCEEDINGS PENDING ARBITRATION

The Federal Arbitration Act of February 12, 1923 (9 USC §1 et seq.) is not applicable to actions maintained, as is this cause, pursuant to §301 of the National Labor Management Relations Act of 1947, Pub. Law 101 80th Cong. C. 120. Colonial Hardwood Flooring Co. v. International Union United Furniture Workers of America, et al. 76 Fed. Supp. 493.

The motion to stay proceedings is denied.

Dated: May 12, 1948.

LOUIS E. GOODMAN,

United States District Judge.

[Endorsed]: Filed May 12, 1948. [14]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that the National Union of Marine Cooks and Stewards, an unincorporated association, defendant above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the order of the above entitled court denying motion to stay proceedings pending arbitration, entered in this action on the 12th day of May, 1948.

Dated this 25th day of May, 1948.

GLADSTEIN, ANDERSEN,

RESNER & SAWYER,

By /s/ RICHARD GLADSTEIN,

By /s/ NORMAN LEONARD,

Attorneys for Defendant.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 9, 1948. [15]

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

Comes now National Union of Marine Cooks and Stewards, an unincorporated association, defendant and appellant herein, and designates the following as the record on appeal in the above-entitled matter:

1. Amended Complaint for Damages, for breach of contract under the Labor-Management Relations Act of 1947, filed herein on January 28, 1948.

2. Motion for Stay of Proceedings filed herein on April 2, 1948.

3. Order Denying Motion to Stay Proceedings Pending Arbitration, filed herein May 12, 1948.

4. Notice of Appeal, filed herein June 9, 1948.

5. This Designation of Record on Appeal, dated June 11, 1948.

Dated: June 11, 1948.

GLADSTEIN, ANDERSEN,
RESNER & SAWYER,

By /s/ RICHARD GLADSTEIN,

By /s/ NORMAN LEONARD,
Attorneys for Defendant.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 12, 1948. [16]

[Title of District Court and Cause.]

DESIGNATION BY PLAINTIFF AND RE-
SPONDENT OF ADDITIONAL PORTIONS
OF RECORD ON APPEAL.

Plaintiff and respondent, Luckenbach Steamship Company, hereby designates the following portions of the record in the above action in addition to those designated by defendant and appellant in its Designation of Record on Appeal on file herein.

1. All of Exhibit A attached to the Amended Complaint on file herein.

2. This Designation by Plaintiff and Respondent of Additional Portions of Record on Appeal.

Dated: June 18, 1948.

BROBECK, PHLEGER &
HARRISON,

By ROBERT E. BURNS,
Attorneys for Plaintiff and
Respondent.

(Acknowledgment of receipt of copy.)

[Endorsed]: Filed June 18, 1948. [17]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET

Good cause appearing therefor, it is hereby ordered that the Appellant herein may have to and including August 28, 1948, to file the Record on Appeal in the United States Circuit Court of Appeals in and for the Ninth Circuit.

Dated: July 19, 1948.

DAL M. LEMMON,
United States District Judge.

[Endorsed]: Filed July 19, 1948. [18]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET

Good cause appearing therefor, it is hereby ordered that the Appellants herein, may have to and including September 7, 1948, to file the Record on Appeal in the United States Circuit Court of Appeals in and for the Ninth Circuit.

Dated: August 26, 1948.

MICHAEL J. ROCHE,
United States District Judge.

[Endorsed]: Filed Aug. 26, 1948. [19]

District Court of the United States, Northern
District of California

CLERK'S CERTIFICATE

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 19 pages, numbered from 1 to 19, inclusive, contain a full, true and correct transcript of the records and proceedings in the case of Luckenbach Steamship Company, Plaintiff, vs. National Union of Marine Cooks and Stewards, an unincorporated association, Defendant, No. 27862-G, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and

certifying the foregoing transcript of record on appeal is the sum of \$6.90 and that the said amount has been paid to me by the Attorney for the appellant herein.

In witness whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 4th day of September, A.D. 1948.

(Seal)

C. W. CALBREATH,
Clerk.

[Endorsed]: No. 12058. United States Court of Appeals for the Ninth Circuit. National Union of Marine Cooks and Stewards, an unincorporated association, Appellant, vs. Luckenbach Steamship Company, a corporation, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed October 7, 1948.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for
the Ninth Circuit.

No. 12060

United States
Court of Appeals
for the Ninth Circuit

ANNA HARRIS and MORRIS HARRIS,
Petitioners,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of The Tax Court
of the United States

NOV 3 1948

PAUL P. O'BRIEN,

No. 12060

United States
Court of Appeals
for the Ninth Circuit

ANNA HARRIS and MORRIS HARRIS,
Petitioners,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of The Tax Court
of the United States

THE

Journal of the

ROYAL SOCIETY OF MEDICINE

Volume 100, Part 1, January 2007

Editorial Board: Sir John Peel, President of the Royal Society of Medicine, and
Prof. Sir John Peel, President of the Royal Society of Medicine, and

Journal of the

ROYAL SOCIETY OF MEDICINE

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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APPEARANCES

For Petitioner:

D. WEBSTER EGAN

DANA LATHAM

For Respondent:

T. M. MATHER

Docket No. 12984

ANNA HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Docket No. 12985

MORRIS HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1947

Jan. 31—Petition received and filed. Taxpayer notified. Fee paid.

Jan. 31—Copy of petition served on General Counsel.

Mar. 25—Answer filed by General Counsel.

1947

Mar. 25—Request for hearing in Los Angeles, California filed by General Counsel.

Mar. 27—Notice issued placing proceeding on Los Angeles, Calif. calendar. Service of answer and request made.

Dec. 8—Hearing set Jan. 26, 1948, Los Angeles.

1948

Jan. 29—Hearing had before Judge Harron on merits. Motion of counsel to consolidate granted. Petitioner allowed ten days to amend petition (see record). Appearance of Dana Latham, Esq. filed. Briefs due 3/16/48; replies due 4/16/48.

Feb. 10—Motion for leave to file the attached amended petition, amended petition lodged, filed by taxpayer.

Feb. 11—Motion for leave to file the attached amended petition granted, amended petition filed.

Feb. 12—Copy of motion and amended petition served on General Counsel.

Feb. 20—Transcript of hearing 1/29/48 filed.

Mar. 2—Answer to amended petition filed by General Counsel. 3/4/48 Copy served.

Mar. 15—Brief filed by taxpayer. 3/17/48 Copy served.

Mar. 16—Brief filed by General Counsel.

Apr. 12—Motion for extension to May 16, 1948 to file reply briefs filed by taxpayer.

1948

Apr. 13—Order, both parties time to file reply briefs extended to April 30th, entered.

Apr. 29—Reply brief filed by taxpayer. Copy served. [1 *]

May 12—Findings of fact and opinion rendered, Judge Harron. Decision will be entered for the respondent. 5/12/48 Copy served.

May 12—Decision entered, Judge Harron, Div. 13.

Aug. 4—Petition for review by U.S. Circuit Court of Appeals for the Ninth Circuit filed by taxpayer.

Aug. 4—Proof of service filed by taxpayer.

Aug. 6—Designation of contents of record on appeal and statement of points filed by taxpayer.

Aug. 6—Notice of filing designation of record and statement of points with affidavit of service by mail attached thereto filed by taxpayer.

Aug. 12—Designation of additional portions of record filed by General Counsel.

Aug. 24—Proof of service and agreement of designation of additional portions of record filed. [2]

* Page numbering appearing at foot of page of original certified Transcript of Record.

Tax Court of the United States

Docket No. 12984

ANNA HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby appeals from the determination of the Commissioner of Internal Revenue, set forth in his deficiency letter (LA-IT-90-d-LHP), dated December 5th, 1946, and as the basis of her appeal sets forth the following:

I.

That petitioner is a resident of the City of Los Angeles, County of Los Angeles, State of California.

II.

That the deficiency letter (a copy of which is attached), was mailed petitioner on December 5th, 1946, and states a deficiency of \$23,799.40.

III.

That the taxes in controversy are Federal Income and Victory taxes for the years 1943 and 1944.

IV.

That the determination of the taxes contained in said deficiency letter is based upon the following errors:

(a) That respondent proposes to add to tax-

payer's net income for the year 1943, the sum of \$23,807.04, said amount being the income of Albert Harris, son of taxpayer and received by the said named Albert Harris, from his undivided one-sixteenth interest of his distributive [5] share of the net income of the Union Mfg. Company, a partnership.

(b) Respondent maintains that the said named Albert Harris, is not a partner as such of the Union Mfg. Company.

(c) Respondent maintains that the net income derived from said named partnership is the community income of taxpayer and Morris Harris, her husband.

(d) Respondent proposes to disallow the sum of \$25,256.18, California income tax as a deduction in computing Victory Tax net income for the year 1943.

(e) Respondent proposes to add to taxpayer's net income for the year 1944, the sum of \$14,590.86, said amount being the income of Albert Harris, son of taxpayer, and received by the said named Albert Harris, from his undivided one-sixteenth interest of his distributive share of the net income of the Union Mfg. Company, a partnership.

(f) Respondent maintains that the said named Albert Harris, is not a partner as such of the Union Mfg. Company.

(g) Respondent maintains that the income derived from said named partnership is the community income of taxpayer and Morris Harris, her husband.

V.

The facts upon which petitioner relies as the basis of her appeal are as follows:

That on January 2nd, 1943, and for many years prior thereto taxpayer and Morris Harris, her husband were associated as co-partners doing business under the firm name of the Union Mfg. Company.

That on or about January 2nd, 1943, taxpayer as the owner of an undivided one-half interest in and to the property and assets of the Union Mfg. Company, a partnership, conveyed, transferred and delivered [6] to Albert Harris, her son, by way of gift, an undivided one-sixteenth interest in and to the property and assets of the Union Mfg. Company. That taxpayer paid to the Collector of Internal Revenue at Los Angeles, California, the gift tax due covering said mentioned gift.

That for the calendar year 1943, the said named Albert Harris, received as his distributive share of the net income of the Union Mfg. Company, the sum of \$23,807.04, and the said named Albert Harris, paid to the Collector of Internal Revenue at Los Angeles, California, Federal Income and Victory Taxes due thereon.

That for the calendar year 1943, taxpayer charged as a deduction the sum of \$25,256.18, income tax paid to the State of California, for the purpose of arriving at Victory Tax Net Income.

That for the calendar year 1944, the said named Albert Harris, received as his distributive share of

the net income of the Union Mfg. Company, the sum of \$14,590.86, and the said named Albert Harris, paid the Collector of Internal Revenue at Los Angeles, California, the Federal Income Tax due thereon.

Wherefore, petitioner prays that respondent take nothing by reason of his determination in respect to the income of Albert Harris, and Victory Tax calculation.

ANNA HARRIS,

Petitioner.

D. WEBSTER EGAN,

Attorney for Petitioner.

State of California,
County of Los Angeles—ss.

Anna Harris, being first duly sworn, on oath [7] deposes and says; that she is the petitioner in the above-entitled appeal; that she has read the foregoing petition and knows the contents thereof; that the same is true of her own knowledge, except as to the matters which are therein stated on information and belief and as those matters that she believes it to be true.

ANNA HARRIS,

Petitioner.

Subscribed and sworn to before me this 8th day of January, 1947.

FRANK LOBER,

Notary Public in and for the County of Los Angeles, State of California.

[8]

Treasury Department
Internal Revenue Service
417 South Hill Street
Los Angeles 13, California

Office of Internal Revenue Agent in Charge Los
Angeles Division

LA:IT:90D:LHB

December 5, 1946

Mrs. Anna Harris
10398 Sunset Boulevard
Los Angeles 24, California

Dear Mrs. Harris:

You are advised that the determination of your income and victory tax liability for the taxable years ended December 31, 1943 and 1944, discloses deficiency of \$23,799.40, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and for-

ward it to the Internal Revenue Agent in Charge, Los Angeles, California, for the attention of L.A. Conf. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,
Commissioner,

By /s/ GEORGE D. MARTIN,
Internal Revenue Agent in Charge.

LHP:vac

Enclosures: Statement Form of Waiver. [9]

STATEMENT

LA:IT:90D:LHP

Mrs. Anna Harris,
10398 Sunset Boulevard,
Los Angeles 24, California.

Tax Liability for the Taxable Years Ended
December 31, 1943 and 1944

Year	Deficiency
1943 Income and victory tax.....	\$ 5,682.73
1944 Income tax	18,136.67
Total.....	<hr/> \$23,799.40

In making this determination of your income and victory tax liability careful consideration has been given to the report of examination dated August 20, 1945, to your protest dated November 5, 1945, and to the statements made at the conferences held.

A copy of this letter and statement has been mailed to your representative, Mr. D. Webster Egan, 403 West Eighth Street, Los Angeles 14, California, in accordance with the authorization contained in the power of attorney executed by you.

The family partnership of Union Manufacturing Company is held to be ineffective for income tax purposes and the income reported in the returns of the said partnership for the years 1943 and 1944 as adjusted herein is held to be the community property of you and your husband.

The dependency credit claimed in your husband's returns for the years 1942, 1943 and 1944 for your brother, Henry S. Cohn, is transferred to your return inasmuch as it has been determined that you furnished his chief support during the years under review. [10]

Adjustment to Net Income

Taxable Year Ended December 31, 1942

Net income as disclosed by return.....	\$215,785.09
Unallowable deduction:	
(a) Loss from rentals decreased.....	477.98
	<hr/>
Net income adjusted.....	\$216,263.07

Explanation of Adjustment

(a) In the rental schedule of your return you claimed a deduction of \$628.56 for depreciation, repairs, and taxes and other expenses incurred in connection with the home which you furnish rent-free to your brother, Henry C. Cohn. Of this amount, \$150.58 expended for taxes represents an allowable deduction under section 23(c) of the Internal Revenue Code. The balance, or \$477.98, is disallowed as not representing a proper deduction under section 23(a) of the Internal Revenue Code.

Computation of Tax

Taxable Year Ended December 31, 1942

Net Income Adjusted		\$216,263.07
Less: Personal exemption (claimed by husband)	\$ 0.00	
Credits for dependents.....	350.00	350.00
	<hr/>	<hr/>
Balance (surtax net income).....		\$215,913.07
Less: Earned income credit (10% of \$3,000.00).....		300.00
		<hr/>
Net income subject to normal tax.....		\$215,613.07
Normal tax at 6% on \$215,613.07.....	\$ 15,936.78	
Surtax on \$215,913.07.....	152,188.72	
	<hr/>	
Correct income tax		\$165,125.50

Adjustments to Net Income

Taxable Year Ended December 31, 1943

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return.....	\$137,322.14	\$143,247.29
Unallowable deductions and ad- ditional income:		
(a) Net gain from sale of capital assets	88.14	0.00
(b) Loss from rentals decreased.....	542.06	690.02
(c) Partnership income decreased....	23,630.76	23,630.76
(d) "Other deductions" disallowed	0.00	25,256.18
Total.....	\$161,583.10	\$192,824.25
Additional deduction:		
(e) Contributions increased	798.60	0.00
Net income adjusted	\$160,784.50	\$192,824.25

Explanation of Adjustments

(a) There is added to income the amount of \$88.14 representing your community share of a net gain from the sale of capital assets realized by the partnership Union Manufacturing Company, computed as follows:

	Total Income	Taxable Income	Your community share—50%
Ordinary net income, as adjusted in (c)....	\$380,560.02	\$380,560.02	\$190,280.01
Long-term capital gain (50% taxable)...	352.56	176.28	88.14
Totals.....	\$380,912.58	\$380,736.30	\$190,368.15

As previously explained, it is held that the income of this partnership is taxable to you and your husband as community income.

(b) For the reason previously explained, the deduction of \$690.02 claimed for repairs, taxes, depreciation and other [12] expenses incurred in connection with the home occupied by your brother, is disallowed to the extent of \$542.06 for income tax net income purposes. The entire amount, or \$690.02, is disallowed for the purpose of the victory tax net income. Taxes paid in the amount of \$147.96, included therein, while allowable for income tax net income under section 23(c) of the Internal Revenue Code, do not represent an allowable deduction from victory tax net income under section 451(a) of the Code.

(c) Your share of the ordinary net income of the partnership, Union Manufacturing Company, held to represent community income as previously stated, is increased by the amount of \$23,630.76, computed as follows:

Ordinary net income as shown in partnership return	\$380,912.58
Less: Amount determined to be net gain from the sale of capital assets.....	352.56
<hr/>	
Ordinary net income adjusted.....	\$380,560.02
Your community share	\$190,280.01
Amount reported in your return.....	166,649.25
<hr/>	
Increase.....	\$ 23,630.76

(d) The deduction of \$25,256.18 claimed for California income tax is disallowed as not representing a proper deduction in computing victory tax net in-

come under section 451(a) of the Internal Revenue Code.

(e) You are allowed an additional deduction of \$798.60 for contributions, representing your community share of contributions made by the partnership, Union Manufacturing Company, which were claimed, and disallowed, on the returns of your son and daughter. Since the income of such partnership is held to be the community income of you and your husband, as previously explained, the amount of contributions made by the partnership represents a community deduction, allowable to you and your husband. [13]

Computation of Alternative Tax

Taxable Year Ended December 31, 1946

Net income adjusted		\$160,784.50
Less: Excess of net long-term capital gain over net short-term capital loss		88.14
		<hr/>
Ordinary net income		\$160,696.36
Less: Personal exemption (claimed by husband)	\$ 0.00	
Credit for dependents.....	350.00	350.00
		<hr/>
Balance (surtax net income).....		\$160,346.36
Less: Earned income credit.....		300.00
		<hr/>
Balance subject to normal tax.....		\$160,046.36
Normal tax at 6% on \$160,046.36.....	\$ 9,602.78	
Surtax on \$160,346.36.....	107,020.55	
		<hr/>
Partial tax		\$116,623.33
Plus: 50% of \$88.14.....		44.07
		<hr/>
Alternative tax		\$116,667.40

Computation of Income and Victory Tax— Current Tax Payment Act of 1943

Taxable Year Ended December 31, 1943

Income tax net income adjusted.....	\$160,784.50	
Less: Personal exemption (claimed by husband)	\$ 0.00	
Credit for dependents.....	350.00	350.00
		<hr/>
Surtax net income	\$160,434.50	
Less: Earned income credit.....	300.00	
		<hr/>
Income subject to normal tax.....	\$160,134.50	
Normal tax at 6% on \$160,134.50.....	\$ 9,608.07	
Surtax on \$160,434.50.....	107,091.95	
		<hr/>
Total income tax.....	\$116,700.02	
Alternative tax	\$116,667.40	
Net income tax.....	\$116,667.40	
Victory tax net income adjusted.....	\$192,824.25	
Less: Specific exemption.....	624.00	
		<hr/>
Income subject to victory tax.....	\$192,200.25	
Victory tax before credit (5% of \$192,200.25)	\$ 9,610.01	
Less: Victory tax credit (42%) limited to	600.00	
		<hr/>
Net victory tax.....	9,010.01	
		<hr/>
1. Net income tax and victory tax.....	\$125,677.41	
2. Income tax for 1942.....	165,125.50	
3. Amount of item 1 or 2, whichever is larger.....	165,125.50	
4. Forgiveness feature:		
(a) Amount of item 1 or 2, which- ever is smaller	\$125,677.41	
(b) Amount forgiven ($\frac{3}{4}$ of (a))	94,258.06	
		<hr/>
(c) Amount unforgiven	31,419.35	
		<hr/>
5. Correct income and victory tax liability (item 3 plus item 4(c)).....	\$196,544.85	
6. Income and victory tax liability shown on re- turn, account No. 909865.....	190,882.12	
		<hr/>
7. Deficiency of income and victory tax	\$ 5,662.73	

Adjustments to Net Income

Taxable Year Ended December 31, 1944

Net income as disclosed by return.....	\$ 92,116.88
Unallowable deduction and additional income:	
(a) Loss from rentals decreased.....	\$ 353.76
(b) Partnership income increased....	20,495.66 20,849.42
	<hr/>
Total.....	\$112,966.30
Additional deduction:	
(c) Contributions increased	469.71
	<hr/>
Net income adjusted	\$112,496.59

Explanation of Adjustments

(a) For the reason previously explained, the deduction of \$503.55 claimed for repairs, taxes, depreciation and other expenses incurred in connection with the home occupied by your brother, is disallowed to the extent of \$353.76.

(d) Your community share of the net income of the partnership, Union Manufacturing Co., is increased by the amount of \$20,495.66, computed as follows:

Ordinary net income, as shown in partner-	
ship return	\$233,453.77
Add: Repairs disallowed as represent-	
ing capital expenditures	\$ 12,048.25
Less: Depreciation allowable.....	238.66
	<hr/>
Net disallowance	11,809.59
	<hr/>
Ordinary net income adjusted.....	\$245,263.36
Your community share.....	\$122,631.68
Amount reported in your return.....	102,136.02
	<hr/>
Increase	\$ 20,495.66

The increase, or \$20,495.66, is added to income for the reason previously given.

(c) You are allowed an additional deduction of \$469.71 for contributions, representing your community share of contributions made by the partnership, Union Manufacturing Company, which were claimed on the returns of your son and daughter and, which have been disallowed to them for the reason previously given. [16]

Computation of Income Tax

Taxable Year Ended December 31, 1944

Net income, adjusted	\$112,496.59	
Less: Surtax exemptions	1,000.00	
		<hr/>
Surtax net income.....	\$111,496.59	
Surtax		\$ 77,551.97
Net income adjusted	\$112,496.59	
Less: Normal-tax exemption	500.00	
		<hr/>
Balance subject to normal tax.....	\$111,996.59	
Normal tax at 3%.....		3,359.90
		<hr/>
Correct income tax liability.....		\$ 80,911.87
Income tax liability shown on return.....		62,775.20
		<hr/>
Deficiency of income tax.....		\$ 18,136.67

[Endorsed]: T.C.U.S. Filed Jan. 31, 1947. [17]

[Title of Tax Court and Cause No. 12984.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I, II and III.

Admits the allegations contained in paragraphs I, II and III of the petition.

IV.

(a) to (g), inclusive. Denies that respondent erred as alleged in subparagraphs (a) to (g), inclusive, of paragraph IV of the petition.

V.

Admits the allegations contained in the first unnumbered subparagraph of paragraph V of the petition. [18]

Denies the allegations contained in the second and third unnumbered subparagraphs of paragraph V of the petition.

Admits the allegations contained in the fourth unnumbered subparagraph of paragraph V of the petition.

Denies the allegations contained in the fifth unnumbered subparagraph of paragraph V of the petition.

VI.

Denies each and every allegation contained in

the petition not hereinbefore specifically admitted or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel.

E. C. CROUTER,
A. J. HURLEY,
Special Attorneys,
Bureau of Internal Revenue.

AJH/ftc 3/17/47

[Endorsed]: T.C.U.S. Filed Mar. 25, 1947. [19]

[Title of Tax Court and Cause No. 12984.]

AMENDED PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (LA:IT:90D:LHP) dated December 5, 1946, and as a basis of this proceeding alleges as follows:

I.

Petitioner is an individual residing at 10398 Sunset Boulevard, Los Angeles 24, California.

II.

The notice of deficiency, a copy of which is attached hereto and marked Exhibit "A", was mailed to petitioner on December 5, 1946.

III.

The taxes in controversy are income and victory [20] taxes for the calendar year 1943 and income tax for the calendar year 1944 as follows:

1943	\$ 5,662.73
1944	18,136.67
<hr/>	
Total	\$23,799.40

IV.

The determination of tax set forth in said notice of deficiency is based upon the following errors:

1. The respondent erred in increasing petitioner's net taxable income for the calendar year 1943 in the amount of \$23,630.76, or any amount, alleged to represent the increase in petitioner's distributive share of the income of the partnership Union Manufacturing Company, of which petitioner was a partner during the calendar year 1943.

2. Respondent erred in disallowing as a deduction in computing petitioner's net income subject to Victory Tax for the calendar year 1943 \$25,256.18, representing California personal income taxes paid by petitioner to the State of California during said year 1943.

3. Respondent erred in determining that a true partnership for all purposes, including the deter-

mination of federal income tax liability did not exist during the calendar year 1943 between petitioner, Morris Harris, Albert P. Harris and Betty Harris. [21]

4. Respondent erred in determining that there was any deficiency in income and/or victory tax for the calendar year 1943.

5. The respondent erred in increasing petitioner's net taxable income for the calendar year 1944 in the amount of \$14,590.86, or any amount in excess of \$5,904.80, alleged to represent the increase in petitioner's distributive share of the income of the partnership Union Manufacturing Company, of which petitioner was a partner during the calendar year 1944.

6. Respondent erred in determining that a true partnership for all purposes, including the determination of federal income tax liability did not exist during the calendar year 1944 between petitioner, Morris Harris, Albert P. Harris and Betty Harris.

7. Respondent erred in determining that there was any deficiency in income tax for the calendar year 1944.

V.

The facts upon which petitioner relies as a basis of this proceeding are as follows:

1. For many years prior to January 2, 1943, petitioner and her husband, Morris Harris, were and had been associated together as equal co-partners under the firm name of Union Manufacturing

Company. The validity of [22] said partnership for federal income tax and all other purposes has never been questioned by respondent or any other person.

2. On or about January 2, 1943, petitioner conveyed to Albert P. Harris, son of petitioner and her husband Morris Harris, by way of gift, an undivided 1/16th interest in and to the properties and assets of said partnership, Union Manufacturing Company. Pursuant to said gift, petitioner filed with the Collector of Internal Revenue at Los Angeles, California, appropriate federal gift tax returns and paid the federal gift taxes determined to be due on account of said gift.

3. On or about the same date, January 2, 1943, petitioner's husband, Morris Harris, conveyed to Betty Harris, the daughter of petitioner and her said husband, a 1/16th interest in the properties and assets of said Union Manufacturing Company. Said Morris Harris filed with the Collector of Internal Revenue at Los Angeles, California, appropriate federal gift tax returns covering said gift, and paid the gift tax determined to be due on account of said gift.

4. On or about said date, January 2, 1943, said parties, petitioner herein, her husband Morris Harris, said Albert P. Harris, and Betty Harris, agreed to associate themselves as co-partners and to carry on said business under the name of Union Manufacturing Company. [23] Said Albert P. Harris contributed to said partnership the 1/16th un-

divided interest in the properties and assets of the former partnership, Union Manufacturing Company, acquired by him from his mother by gift as heretofore recited. Said Betty Harris contributed to said partnership the 1/16th undivided interest in the properties and assets of the former partnership, Union Manufacturing Company, acquired by her from her father by gift as heretofore recited. Petitioner herein and her husband, Morris Harris, each contributed their 7/16ths interest in the properties and assets of said Union Manufacturing Company remaining to them after the gifts as aforesaid.

Said co-partners agreed to share profits and losses on the following basis:

Anna Harris	7/16ths
Morris Harris	7/16ths
Albert P. Harris	1/16th
Betty Harris	1/16th

In connection with said partnership there were no restrictions of any kind or nature upon the activities, rights of withdrawal, etc., of any of the partners.

5. Throughout the calendar years 1943 and 1944 said partnership, composed of the four persons above referred to, conducted its business and affairs on a partnership basis and filed appropriate federal income tax returns on said basis. Despite this fact respondent [24] erroneously and without warrant in fact or law has ignored said partner-

ship and has charged all the income of said partnership for said calendar years 1943 and 1944 one-half to petitioner herein and one-half to her husband, Morris Harris.

6. During the calendar year 1943 petitioner herein paid to the State of California, as personal income taxes upon her income for the calendar year 1942 the sum of \$25,256.18. In determining her victory tax liability for said calendar year 1943 petitioner deducted the amount of said payment. Respondent erroneously and without warrant in fact or law was refused to allow said deduction in determining petitioner's net income for the calendar year 1943 subject to victory tax.

Wherefore, petitioner prays that this Court may hear this proceeding and determine:

1. That the respondent erred in the particulars set forth in paragraph IV of this petition.

2. That there is no deficiency in income or victory taxes for the calendar year 1943 and no deficiency in income tax for the calendar year 1944.

February 6, 1948.

Respectfully submitted,

/s/ D. WEBSTER EGAN,

/s/ DANA LATHAM,

Counsel for Petitioner.

[Verified.] [25]

[Clerk's Note: Exhibit "A", Notice of Deficiency, is attached to original Petition and is not reproduced here.]

[Title of Tax Court and Cause No. 12984.]

ANSWER TO AMENDED PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the amended petition.

IV (1) to (7), inclusive. Denies that the Commissioner erred in the determination of the deficiencies as alleged in paragraph IV of the amended petition and subparagraphs (1) to (7), inclusive, thereunder.

V (1). Admits the allegations contained in subparagraph (1) of paragraph V of the amended petition.

V (2). Admits that petitioner filed with the Collector of Internal Revenue at Los Angeles, California, federal gift tax returns, but denies the remaining allegations contained in subparagraph (2) of paragraph V of the amended petition. [36]

V (3). Admits that Morris Harris filed with the Collector of Internal Revenue at Los Angeles, California, federal gift tax returns, but denies the remaining allegations contained in subparagraph (3) of paragraph V of the amended petition.

V (4) and (5). Denies the allegations contained

in subparagraphs (4) and (5) of paragraph V of the amended petition.

V (6). Admits that during the calendar year 1943 petitioner herein paid to the State of California, as personal income taxes upon her income for the calendar year 1942 the sum of \$25,256.18; that in determining her victory tax liability for said calendar year 1943 petitioner deducted the amount of said payment; that respondent has refused to allow said deduction in determining petitioner's net income for the calendar year 1943 subject to victory tax, but denies the remaining allegations contained in subparagraph (6) of paragraph V of the amended petition.

VI. Denies generally and specifically each and every allegation in the amended petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
E. C. CROUTER,
T. M. MATHER,
Special Attorneys,

TMM:b 2/25/48 Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Mar. 2, 1948. [37]

Tax Court of the United States

Docket No. 12985

MORRIS HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby appeals from the determination of the Commissioner of Internal Revenue, set forth in his deficiency letter (LA-IT-90-D-LHP), dated December 5th, 1946, and as the basis of his appeal sets forth the following:

I.

That petitioner is a resident of the City of Los Angeles, County of Los Angeles, State of California.

II.

That the deficiency letter (a copy of which is attached), was mailed petitioner on December 5th, 1946, and states a deficiency of \$24,728.97.

III.

That the taxes in controversy are Federal Income and Victory Taxes for the years 1943 and 1944.

IV.

That the determination of the taxes contained in said deficiency letter is based upon the following errors:

(a) That respondent proposes to add to taxpayer's net income for the year 1943, the sum of \$23,807.04, said amount being the income of Betty Harris, daughter of taxpayer and received by the said named Betty Harris, from her undivided one-sixteenth interest of her distributive [38] share of the net income of the Union Manufacturing Company, a partnership.

(b) Respondent maintains that the said named Betty Harris, is not a partner as such of the Union Manufacturing Company.

(c) Respondent maintains that the net income derived from said named partnership is the community income of taxpayer and Anna Harris, his wife.

(d) Respondent proposes to disallow the sum of \$26,747.65, California income tax as a deduction in computing Victory Tax net income for the year 1943.

(e) Respondent proposes to add to taxpayer's net income for the year 1944, the sum of \$14,590.86, said amount being the income of Betty Harris, daughter of taxpayer, and received by the said named Betty Harris, from her undivided one-sixteenth interest of her distributive share of the net income of the Union Manufacturing Company, a partnership.

(f) Respondent maintains that the said named Betty Harris, is not a partner as such of the Union Manufacturing Company.

(g) Respondent maintains that the income derived from said named partnership is the community income of taxpayer and Anna Harris, his wife.

V.

The facts upon which petitioner relies as the basis of his appeal are as follows:

That on January 2nd, 1943, and for many years prior thereto taxpayer and Anna Harris, his wife, were associated as co-partners doing business under the firm name of the Union Manufacturing Company.

That on or about January 2nd, 1943, taxpayer as the owner of an undivided one-half interest in and to the property and assets of the Union Manufacturing Company, a partnership, conveyed, transferred and delivered [39] to Betty Harris, his daughter, by way of gift, an undivided one-sixteenth interest in and to the property and assets of the Union Manufacturing Company. That taxpayer paid to the Collector of Internal Revenue at Los Angeles, California, the gift tax due covering said mentioned gift.

That for the calendar year 1943, the said named Betty Harris, received as her distributive share of the net income of the Union Manufacturing Company, the sum of \$23,807.04, and the said named Betty Harris, paid to the Collector of Internal Revenue at Los Angeles, California, Federal Income and Victory Taxes due thereon.

That for the year 1943, taxpayer charged as a deduction the sum of \$26,747.65, income tax paid to the State of California, for the purpose of arriving at Victory Tax Net Income.

That for the calendar year 1944, the said named Betty Harris, received as her distributive share of the net income of the Union Manufacturing Company, the sum of \$14,590.86, and the said named Betty Harris, paid to the Collector of Internal Revenue at Los Angeles, California, the Federal Income Tax due thereon.

Wherefore, petitioner prays that respondent take nothing by reason of his determination except the tax due covering the disallowance of certain building repairs.

MORRIS HARRIS,

Petitioner.

D. WEBSTER EGAN,

Attorney for Petitioner.

State of California,
County of Los Angeles—ss.

Morris Harris, being first duly sworn, on oath, deposes and says; that he is the petitioner in the above-entitled appeal; [40] that he has read the foregoing petition and knows the contents thereof; that the same is true of his own knowledge, except as to the matters which are therein stated on in-

formation and belief and as those matters that he believes it to be true.

MORRIS HARRIS,
Petitioner.

Subscribed and sworn to before me this 8th day
of January, 1947.

FRANK LOBER,
Notary Public in and for the County of Los An-
geles, State of California. [41]

Treasury Department
Internal Revenue Service

417 South Hill Street
Los Angeles 13, California

Office of Internal Revenue Agent in Charge Los
Angeles Division

LA:IT:90D:LHP

Dec. 5, 1946

Mr. Morris Harris
10398 Sunset Boulevard
Los Angeles 24, California

Dear Mr. Harris:

You are advised that the determination of your
income and victory tax liability for the taxable
years ended December 31, 1943 and 1944 discloses
a deficiency of \$24,728.97, as shown in the statement
attached.

In accordance with the provisions of existing in-

ternal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Los Angeles, California, for th attention of LA:Conf. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,
Commissioner,

By /s/ GEORGE D. MARTIN,
Internal Revenue Agent in Charge.

LHP:vmc

Enclosures: Statement, Form of Waiver. [42]

STATEMENT

LA:IT:90D:LHP

Mr. Morris Harris,
10398 Sunset Boulevard,
Los Angeles 24, California.

Tax Liability for the Taxable Years Ended
December 31, 1943 and 1944

Year	Deficiency
1943 Income and victory tax.....	\$ 6,035.87
1944 Income tax	18,693.10
Total.....	<u>\$24,728.97</u>

In making this determination of your income and victory tax liability careful consideration has been given to the report of examination dated August 20, 1945, to your protest dated November 5, 1945, to the statements made at the conferences held, and to your claim for refund filed on April 13, 1945, for the year 1944.

A copy of this letter and statement has been mailed to your representative, Mr. D. Webster Egan, 403 West Eighth Street, Los Angeles 14, California, in accordance with the authorization contained in the power of attorney executed by you.

The issue raised in your claim for refund for the taxable year ended December 31, 1944, relative to that portion of your distributable income reported from the partnership "Union Ranch", which represents gain from the sale or exchange of capital assets held for more than six months, is conceded and appropriate adjustments therefor is made herein.

The family partnership of Union Manufacturing Company is held to be ineffective for income tax purposes and the income reported in the returns of the said partnership for the years 1943 and 1944 as adjusted herein is held to be the community property of you and your wife. [43]

The dependency credit claimed in your returns for the years 1942, 1943 and 1944 for your brother-in-law, Henry S. Cohn, is transferred to the return of your wife inasmuch as it has been determined that she furnished his chief support during the years under review.

Adjustment to Net Income

Taxable Year Ended December 31, 1942

Net income as disclosed by return.....	\$228,931.78
Unallowable deductions:	
(a) Gasoline tax	45.75
	<hr/>
Net income adjusted	\$228,977.53

Explanation of Adjustment

(a) The deduction of \$45.75 for gasoline taxes paid to the State of California is disallowed as not representing taxes deductible under section 23(c) of the Internal Revenue Code.

Computation of Tax

Taxable Year Ended December 31, 1942

Net Income Adjusted		\$228,977.53
Less: Personal exemption.....	\$1,200.00	
Credit for dependents.....	700.00	1,900.00
		<hr/>
Balance (surtax net income).....		\$227,077.53
Less: Earned income credit (10% of \$14,000.00).....		1,400.00
		<hr/>
Net income subject to normal tax.....		\$225,677.53
Normal tax at 6% on \$225,677.53.....	\$ 13,540.65	
Surtax on \$227,077.53.....	161,343.57	
		<hr/>
Correct income tax.....		\$174,884.22

Adjustments to Net Income

Taxable Year Ended December 31, 1943

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return.....	\$148,201.50	\$156,171.72
Additional income:		
(a) Net gain from sale of capital assets	88.14	
(b) Partnership income increased.....	23,630.76	23,630.76
(c) Taxes	0.00	26,747.65
	<hr/>	<hr/>
Total.....	\$171,920.40	\$206,550.13
Additional deduction:		
(d) Contributions increased	798.60	0.00
	<hr/>	<hr/>
Net income adjusted.....	\$171,121.80	\$206,550.13

Explanation of Adjustments

(a) There is added to income the amount of \$88.14 representing your community share of a net gain from the sale of capital assets realized by the part-

nership Union Manufacturing Company, computed as follows:

	Total Income	Taxable Income	Your community share—50%
Ordinary net income, as adjusted in (b).....	\$380,560.02	\$380,560.02	\$190,280.01
Long-term capital gain (50% taxable)	352.56	176.28	88.14
Totals.....	\$380,912.58	\$380,736.30	\$190,368.15

As previously explained, it is held that the income of this partnership is taxable to you and your wife as community income.

(b) Your share of the ordinary net income of the partnership, Union Manufacturing Company, held to represent community income as previously stated, is increased by the amount of \$23,630.76, computed as follows: [45]

Ordinary net income as shown in partnership return.....	\$380,912.58
Less: Amount determined to be net gain from the sale of capital assets.....	352.56
Ordinary net income adjusted.....	\$380,560.02
Your community share.....	\$190,280.01
Amount reported in your return.....	166,649.25
Increase	\$ 23,630.76

(c) The deduction of \$26,747.65 claimed for California income tax is disallowed as not representing a proper deduction in computing victory tax net income under section 451(a) of the Internal Revenue Code.

(d) You are allowed an additional deduction of \$798.60 for contributions, representing your community share of contributions made by the partnership, Union Manufacturing Company, which were

claimed, and disallowed, on the returns of your son and daughter. Since the income of such partnership is held to be the community income of you and your wife, as previously explained, the amount of contributions made by the partnership represents a community deduction, allowable to you and your wife.

Computation of Alternative Tax

Taxable Year Ended December 31, 1943

Net income adjusted.....	\$171,121.80	
Minus: Excess of net long-term capital gain over net- short-term capital loss		88.14
Ordinary net income.....	\$171,033.66	
Less: Personal exemption	\$1,200.00	
Credit for dependents	700.00	1,900.00
Balance (surtax net income).....	\$169,133.66	
Less: Earned income credit.....		1,400.00
Net income subject to normal tax.....	\$167,733.66	
Normal tax at 6% on \$167,733.66.....	\$ 10,064.02	
Surtax on \$169,133.66	114,138.26	
Partial tax	\$124,202.28	
Plus: 50% of \$88.14.....		44.07
Alternative tax		124,246.35

Computation of Income and Victory Tax—Current Tax Payment Act of 1943

Taxable Year Ended December 31, 1943

Income tax net income adjusted.....	\$171,121.80
Less: Personal exemption.....	\$1,200.00
Credit for dependents.....	700.00
	<hr/> 1,900.00
Surtax net income	\$169,221.80
Less: Earned income credit.....	1,400.00
	<hr/>
Income subject to normal tax.....	\$167,821.80
Normal tax at 6% on \$167,821.80.....	\$ 10,069.31
Surtax on \$169,221.80	114,209.66
	<hr/>
Total income tax.....	\$124,278.97
Alternative tax	\$124,246.35
Net income tax.....	\$124,246.35
Victory tax net income adjusted.....	\$206,550.13
Less: Specific exemption	624.00
	<hr/>
Income subject to victory tax.....	\$205,926.13
Victory tax before credit (5% of \$205,926.13)	\$ 10,296.31
Less: Victory Tax credit.....	700.00
	<hr/>
Net victory tax.....	\$ 9,596.31
	<hr/>
1. Net income tax and victory tax.....	\$133,842.66
2. Income tax for 1942.....	\$174,884.22
3. Amount of item 1 or 2, whichever is larger.....	\$174,884.22
4. Forgiveness feature:	
(a) Amount of item 1 or 2, whichever is smaller	\$133,842.66
(b) Amount forgiven ($\frac{3}{4}$ of (a))....	100,382.00
	<hr/>
(c) Amount unforgiven	33,460.66
5. Correct income and victory tax liability (item 3 plus item 4(c)).....	\$208,344.88
6. Income and victory tax liability shown on return, account No. 909866.....	202,309.01
	<hr/>
7. Deficiency of income and victory tax.....	\$ 6,035.87

Adjustments to Net Income

Taxable Year Ended December 31, 1944

Net income as disclosed by return.....	\$107,498.21
Additional income:	
(a) Net gain from sale of capital assets	\$ 418.48
(b) Partnership income increased....	20,077.17 20,495.65
Total.....	\$127,993.86
Additional deduction:	
(c) Contributions	469.71
Net income adjusted.....	\$127,524.15

Explanation of Adjustments

(a) In your return you reported the amount of \$1,125.98 as representing your distributive share of the ordinary net income of the partnership Union Ranch. In a claim for refund filed by you on April 13, 1945, it is stated that \$418.49 of this amount actually represents your distributive share of a net gain from the sale of capital assets realized by the partnership. The amount of \$418.48, computed as follows, is accordingly added to income, and is eliminated from partnership ordinary net income in adjustment (b): [48]

	Total Income	Taxable Income	Your distributive share—50%
Ordinary net income of partnership	\$1,415.00	\$1,415.00	\$ 707.50
Long-term capital gain (50% taxable)	1,673.93	836.97	418.48
Totals.....	\$3,088.93	\$2,251.97	\$1,125.98

(b) Your community share of the ordinary net income of the partnerships named below is increased by the amount of \$20,077.17, computed as follows:

	Reported	Corrected	Increase (Decrease)
1. Union Manufactur- ing Co.	\$102,136.03	\$122,631.68	\$ 20,495.65
2. Union Ranch	1,125.98	707.50	(418.48)
Totals.....	\$103,262.01	\$123,339.18	\$ 20,077.17

1. As previously stated, it has been determined that the net income of this partnership, adjusted as follows, represents community income:

Ordinary net income, as shown in partnership return..	\$233,453.77
Add: Repairs disallowed as representing capital expenditures	\$ 12,048.25
Less: Depreciation allowable.....	238.66
Net disallowance	11,809.59
Ordinary net income adjusted.....	\$245,263.36
Your community share.....	\$122,631.68
Amount reported in your return.....	\$102,136.03
Increase	\$ 20,495.65

2. See adjustment (a).

[49]

(c) You are allowed an additional deduction of \$469.71 for contributions, representing your community share of contributions made by the partnership, Union Manufacturing Company, which were claimed on the returns of your son and daughter and which have been disallowed to them for the reason previously given.

Computation of Alternative Tax Taxable Year Ended December 31, 1944

Net income adjusted.....	\$127,524.15	
Less: Excess of net long-term capital gain over net short-term capital loss		418.48
Ordinary net income.....	\$127,105.67	
Less: Surtax exemptions.....	1,500.00	
Balance (surtax net income).....	\$125,605.67	
Surtax	\$ 90,109.05	
Ordinary net income.....	\$127,105.67	
Less: Normal-tax exemption	500.00	
Balance subject to normal tax.....	\$126,605.67	
Normal tax at 3%.....		3,798.17
Partial tax	\$ 93,907.22	
Plus: 50% of \$418.48.....		209.24
Alternative tax	\$ 94,116.46	

Computation of Income Tax Taxable Year Ended December 31, 1944

Net income adjusted.....	\$127,524.15	
Less: Surtax exemptions.....	1,500.00	
Surtax net income	\$126,024.15	
Surtax		\$ 90,481.49
Net income adjusted	\$127,524.15	
Less: Normal-tax exemption	500.00	
Balance subject to normal tax.....	\$127,024.15	
Normal tax at 3%.....		3,810.72
Total income tax	\$ 94,292.21	
Total alternative tax.....	\$ 94,116.46	
Correct income tax liability.....	\$ 94,116.46	
Income tax liability shown on return.....	\$ 75,423.36	
Deficiency of income tax—.....	\$ 18,693.10	

[Endorsed]: T.C.U.S. Filed Jan. 31, 1947. [51]

[Title of Tax Court and Cause No. 12985.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I, II and III.

Admits the allegations contained in paragraphs I, II and III of the petition.

IV.

(a) to (g), inclusive. Denies that respondent erred as alleged in subparagraphs (a) to (g), inclusive, of paragraph IV of the petition.

V.

Admits the allegations contained in the first unnumbered subparagraph of paragraph V of the petition. [52]

Denies the allegations contained in the second and third unnumbered subparagraphs of paragraph V of the petition.

Admits the allegations contained in the fourth unnumbered subparagraph of paragraph V of the petition.

Denies the allegations contained in the fifth unnumbered subparagraph of paragraph V of the petition.

VI.

Denies each and every allegation contained in the petition not hereinbefore specifically admitted or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel.

E. C. CROUTER,
A. J. HURLEY,
Special Attorneys,
Bureau of Internal Revenue.

AJH/ftc 3/17/47

[Endorsed]: T.C.U.S. Filed Mar. 25, 1947. [53]

[Title of Tax Court and Cause No. 12985.]

AMENDED PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (LA:IT:90D:LHP) dated December 5, 1946, and as a basis of this proceeding alleges as follows:

I.

Petitioner is an individual residing at 10398 Sunset Boulevard, Los Angeles 24, California.

II.

The notice of deficiency, a copy of which is attached hereto and marked Exhibit "A", was mailed to petitioner on December 5, 1946.

III.

The taxes in controversy are income and victory [54] taxes for the calendar year 1943 and income tax for the calendar year 1944 as follows:

1943	\$ 6,035.87
1944	18,693.10
<hr/>	
Total	\$24,728.97

IV.

The determination of tax set forth in said notice of deficiency is based upon the following errors:

1. The respondent erred in increasing petitioner's net taxable income for the calendar year 1943 in the amount of \$23,630.76, or any amount, alleged to represent the increase in petitioner's distributive share of the income of the partnership Union Manufacturing Company, of which petitioner was a partner during the calendar year 1943.

2. Respondent erred in disallowing as a deduction in computing petitioner's net income subject to victory tax for the calendar year 1943 \$26,747.65, representing California personal income

taxes paid by petitioner to the State of California during said year 1943.

3. Respondent erred in determining that a true partnership for all purposes, including the determination of federal income tax liability did not exist during the calendar year 1943 between petitioner, Anna Harris, Albert P. Harris and Betty Harris. [55]

4. Respondent erred in determining that there was any deficiency in income and/or victory tax for the calendar year 1943.

5. The respondent erred in increasing petitioner's net taxable income for the calendar year 1944 in the amount of \$14,590.86, or any amount in excess of \$5,904.80, alleged to represent the increase in petitioner's distributive share of the income of the partnership Union Manufacturing Company, of which petitioner was a partner during the calendar year 1944.

6. Respondent erred in determining that a true partnership for all purposes, including the determination of federal income tax liability did not exist during the calendar year 1944 between petitioner, Anna Harris, Albert P. Harris and Betty Harris.

7. Respondent erred in determining that there was any deficiency in income tax for the calendar year 1944.

V.

The facts upon which petitioner relies as a basis of this proceeding are as follows:

1. For many years prior to January 2, 1943, petitioner and his wife, Anna Harris, were and had been associated together as equal co-partners under the firm name of Union Manufacturing Company. The validity of said partnership for federal income tax and all other [56] purposes has never been questioned by respondent or any other person.

2. On or about January 2, 1943, petitioner conveyed to Betty Harris, daughter of petitioner and his wife Anna Harris, by way of gift, an undivided 1/16th interest in and to the properties and assets of said partnership, Union Manufacturing Company. Pursuant to said gift, petitioner filed with the Collector of Internal Revenue at Los Angeles, California, appropriate federal gift tax returns and paid the federal gift tax determined to be due on account of said gift.

3. On or about the same date, January 2, 1943, petitioner's wife, Anna Harris, conveyed to Albert P. Harris, the son of petitioner and his said wife, a 1/16th interest in the properties and assets of said Union Manufacturing Company. Said Anna Harris filed with the Collector of Internal Revenue at Los Angeles, California, appropriate federal gift tax returns covering said gift, and paid the gift tax determined to be due on account of said gift.

4. On or about said date, January 2, 1943, said parties, petitioner herein, his wife Anna Harris, said Albert P. Harris and Betty Harris, agreed to associate themselves as co-partners and to carry on said business under the name of Union Manu-

facturing Company. Said [57] Albert P. Harris contributed to said partnership the 1/16th undivided interest in the properties and assets of the former partnership, Union Manufacturing Company, acquired by him from his mother by gift as heretofore recited. Said Betty Harris contributed to said partnership the 1/16th undivided interest in the properties and assets of the former partnership, Union Manufacturing Company, acquired by her from her father by gift as heretofore recited. Petitioner herein and his wife, Anna Harris, each contributed their 7/16ths interest in the properties and assets of said Union Manufacturing Company remaining to them after the gifts as aforesaid.

Said co-partners agreed to share profits and losses on the following basis:

Morris Harris	7/16ths
Anna Harris	7/16ths
Albert P. Harris	1/16th
Betty Harris	1/16th

In connection with said partnership there were no restrictions of any kind or nature upon the activities, rights of withdrawal, etc., of any of the partners.

5. Throughout the calendar years 1943 and 1944 said partnership, composed of the four persons above referred to, conducted its business and affairs on a partnership basis and filed appropriate federal income tax returns on said basis. Despite this fact respondent erroneously and without war-

rant in fact or law has [58] ignored said partnership and has charged all the income of said partnership for said calendar years 1943 and 1944 one-half to petitioner herein and one-half to his wife, Anna Harris.

6. During the calendar year 1943 petitioner herein paid to the State of California, as personal income taxes upon his income for the calendar year 1942 the sum of \$26,747.65. In determining his victory tax liability for said calendar year 1943 petitioner deducted the amount of said payment. Respondent erroneously and without warrant in fact or law has refused to allow said deduction in determining petitioner's net income for the calendar year 1943 subject to victory tax.

Wherefore, petitioner prays that this Court may hear this proceeding and determine:

1. That the respondent erred in the particulars set forth in paragraph IV of this petition.
2. That there is no deficiency in income or victory taxes for the calendar year 1943 and no deficiency in income tax for the calendar year 1944.

February 6, 1948.

Respectfully submitted,

/s/ D. WEBSTER EGAN,

/s/ DANA LATHAM,

Counsel for Petitioner.

(Verified.)

[59]

[Clerk's Note: Exhibit "A", Notice of Deficiency, is attached to original Petition and is not reproduced here.]

[Title of Tax Court and Cause No. 12985.]

ANSWER TO AMENDED PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the amended petition.

IV (1) to (7), inclusive. Denies that the Commissioner erred in the determination of the deficiencies as alleged in paragraph IV of the amended petition and subparagraphs (1) to (7), inclusive, thereunder.

V (1). Admits the allegations contained in subparagraph (1) of paragraph V of the amended petition.

V (2). Admits that petitioner filed with the Collector of Internal Revenue at Los Angeles, California, federal gift tax returns, but denies the remaining allegations contained in subparagraph (2) of paragraph V of the amended petition. [70]

V (3). Admits that Anna Harris filed with the Collector of Internal Revenue at Los Angeles, California, federal gift tax returns, but denies the remaining allegations contained in subparagraph (3) of paragraph V of the amended petition.

V (4) and (5). Denies the allegations contained

in subparagraphs (4) and (5) of paragraph V of the amended petition.

V (6). Admits that during the calendar year 1943 petitioner herein paid to the State of California, as personal income taxes upon his income for the calendar year 1942 the sum of \$26,747.65; that in determining his victory tax liability for said calendar year 1943 petitioner deducted the amount of said payment; that respondent has refused to allow said deduction in determining petitioner's net income for the calendar year 1943 subject to victory tax, but denies the remaining allegations contained in subparagraph (6) of paragraph V of the amended petition.

VI. Denies generally and specifically each and every allegation in the amended petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel.
E. C. CROUTER,
T. M. MATHER,
Special Attorneys,
Bureau of Internal Revenue.

TMM:b 2/25/48

[Endorsed]: T.C.U.S. Filed Mar. 2, 1948. [71]

10 T. C. No. 109

The Tax Court of the United States

Anna Harris, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

Morris Harris, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

Docket Nos. 12984, 12985. Promulgated May 12, 1948.

1. Petitioners are co-partners, carrying on a manufacturing business under the name of Union Manufacturing Company. They have two children. Each own an undivided one-half interest in the business, and entitled to receive one-half of the profits each year. As of January 1, 1943, each petitioner purportedly gave an undivided, one-sixteenth interest in the business to each child. Neither child contributed any capital originating with himself; and during 1943 neither child performed any services in the business. Under the facts, held, that petitioners did not create a new and bona fide partnership in 1943, and that their two children were not co-partners with them in the conduct of the partnership business known as Union Manufacturing Company. *Commissioner vs. Tower*, 327 U. S. 280, followed.

2. Each petitioner paid personal income taxes to the State of California for the year 1942 under the California income tax law. The California income taxes were not paid in connection with the carry-

ing on of a trade or business, or otherwise within the meaning of section 451(a)(3) of the I.R.C. Held, that under the provisions of section 451(a)(3) the amount which is paid for state income taxes is not deductible in computing victory tax net income. [72]

D. Webster Egan, Esq., and Dana Latham, Esq., for the petitioners.

T. M. Mather, Esq., for the respondent.

Respondent has determined deficiencies in income tax as follows:

	1943	1944
Anna Harris, Docket No. 12984.....	\$5,682.73	\$18,136.67
Morris Harris, Docket No. 12985.....	6,035.87	18,693.10

There are two questions presented, whether two children are members of a partnership, and whether income taxes of the State of California are deductible in computing the victory tax net income for the year 1943.

Petitioners filed separate income tax returns with the collector for the sixth district of California.

FINDINGS OF FACT

Morris Harris and Anna Harris are husband and wife. They reside in Los Angeles, California. Albert J. Harris and Betty Harris are children of petitioners. They were nineteen years old and sixteen years old, respectively, in 1943.

Petitioners are associated together as equal co-partners under the firm name of Union Manufacturing Company. They had been associated in part-

nership for many years prior to 1943. Each owns a one-half interest in the partnership and profits, under a written agreement dated April 1, 1937, which covers a term of 10 years.

Union Manufacturing Company has its main plant in Los Angeles. It carries on the business of the manufacture and sale of men's work and sport clothes.

In 1909, Morris Harris began this enterprise. The capital employed has been built up by retaining profits from year to year. Morris Harris is the manager. In [73] 1941 the volume of sales was around \$2,000,000. In 1942, about 400 people were employed in the Los Angeles plant. Union Manufacturing Company had a second place of business in 1942 in El Paso, Texas, where around 100 people were employed; and the employment in El Paso increased to about 300 later. Morris Harris owns the land and building where the Los Angeles plant is located, and it does not appear as an asset in the balance sheet of the firm. In 1942, the Los Angeles plant and real estate had a value of around \$300,000, without equipment. The equipment which is used in the plant consists of all kinds of machinery and sewing machines. In the manufacturing departments there are several floor ladies under one superintendent. The goods manufactured are sold all over the United States. In 1942, the market was limited to the Rocky Mountain and Pacific Coast regions and ten or twelve salesmen were

employed on a commission basis. In 1942, and thereafter, goods were sold in chain stores. Morris receives a salary of about \$200 a week which constitutes a drawing account against his share of the profits.

As of December 31, 1942, the Union Manufacturing Company had assets of \$945,975.23, of which inventory amounted to \$538,992. Liabilities amounted to only \$9,065.40, leaving net assets of \$936,909.83.

As of December 31, 1942, after the addition of one-half of 1942 profits, the balance of the capital account of Morris Harris was \$471,351.04; and the balance of the capital account of Anna Harris was \$465,558.79.

The balance sheet of the partnership as of December 31, 1942, was as follows: [74]

ASSETS

Petty Cash	\$	35.49	
Union Bank & Trust Co.—			
Checking Acct.		166,571.62	
Union Bank & Trust Co.—Payroll Acct.		100.00	
State National Bank—El Paso, Tex.....		7,797.08	
Accounts Receivable—Good		187,880.36	
Accounts Receivable—Doubtful.....		1,788.20	
Loans to Employees		106.73	
Inventory 12/21/42		538,992.70	
Machinery		40,211.68	
Furniture & Fixtures.....		694.09	
Automobile		859.80	
Stationery & Printing.....		400.00	
Prepaid Insurance		537.48	\$945,975.23

LIABILITIES

Employees—Salaries, commissions etc...\$	449.94	
Social Security—Employees	2,240.74	
Social Security—Firm	6,374.72	\$ 9,065.40

CAPITAL

Mr. Harris	\$359,705.94	
Less drawing acct.....\$28,050.00		
Less income tax 1941....	86,238.30	
Less income tax 1940		
(add.)	92.08	114,380.38
		245,325.56
Plus 1/2 1942 profits.....	226,025.48	471,351.04
A. Harris:	\$334,699.14	
Less drawing acct.....\$14,949.35		
Less income tax 1941....	80,216.48	95,165.83
		239,533.31
Plus 1/2 1942 profits.....	226,025.48	465,558.79
		\$945,975.23

The son of petitioners, Albert, finished high school in June 1941; he entered the University of Virginia in the fall of 1941. He continued in the University of Virginia for the academic year 1941-1942, returning to Los Angeles in June of 1942. During the summer of 1942 he attended evening classes at the University of Southern California, where he took special courses in textiles. In September 1942, he entered the textiles school of the University of North Carolina at Raleigh, North Carolina. He returned home for the Christmas holidays of 1942. He enlisted in the Army in [75] December 1942. Thereafter, he returned to Raleigh,

North Carolina, where he remained at the University of North Carolina until April 1943, when he was called for active duty in the armed forces. He was in the service from April 1943 until January 1946. Upon his discharge from the service he returned to Los Angeles and went to work in the business of Union Manufacturing Company.

Betty, petitioners' daughter, attended school during the years 1943 and 1944 at either University High School, Flintridge School or Mills College in California.

In 1942, in the summer months and at Christmas, petitioners discussed the matter of making a gift of an interest in the partnership to their son, and they considered it fair to do the same for their daughter. The arrangement discussed was not carried to any formal agreement; there was no written agreement, and there were no instruments of gifts or assignments or transfers drawn up or executed. In the discussions, Anna Harris was to make gift of part of her partnership interest to her son, Albert, and Morris Harris was to make gift of part of his interest to his daughter, Betty. The gifts were to be made on or about January 2, 1943.

On September 16, 1943, book entries were made in the capital accounts of Anna and Morris Harris, and ledger sheets were made opening capital accounts in the names of Albert and Betty. However, instead of making book entries to show a transfer of an interest from Anna to her son Albert, and

from Morris to his daughter Betty, the entries which were made transferred an amount out of Anna's capital account to Betty, and an amount out of Morris' capital account to Albert. These bookkeeping entries did not correspond with or reflect statements which were made on Form 709, Gift Tax [76] Return, to the effect that Anna Harris had made gift to Albert Harris on January 2, 1943, of an undivided one-sixteenth interest in the property and assets of Union Manufacturing Company; and that Morris Harris had made gift to Betty Harris on January 2, 1943, of an undivided one-sixteenth interest in the property and assets of Union Manufacturing Company.

The two gift tax returns of each petitioner were dated September 27, 1943.

The capital account of Morris Harris, on September 16, 1943, was debited with the amount \$34,083.70, and a capital account in the name of Albert Harris, was credited with the same amount as of January 1, 1943, by a transfer from the capital account of Morris Harris.

The capital account of Anna Harris was debited on September 16, 1943, in the amount of \$34,083.70; and a capital account in the name of Betty Harris was credited with the same amount as of January 1, 1943, by transfer from the capital account of Anna Harris.

Entries were made in the general journal on September 16, 1943, of the same debits and credits from and to capital accounts as were made in the

four respective ledger capital accounts with the notation:

To transfer above interest in company to Albert and Betty Harris, son and daughter, one-sixteenth each, based on M. Harris' interest, \$270,049.36 and A. Harris' interest, \$275,289.73.

The business of Union Manufacturing Company was conducted during 1943 and 1944 in the same way as it had been conducted in 1942 and prior. No services were rendered to or in the business by the children, Albert and Betty, during 1943 and 1944. Neither one of the children contributed any capital of their own to the existing partnership business in 1943 or 1944, or in 1942 or prior. [77]

When, prior to 1943, Albert went to the place of business to do work of some general type which a school boy could do, after school hours and during school vacations, he was not paid any amount.

Neither Albert nor Betty withdrew any sum from the Union Manufacturing Company during 1943 and 1944. However, debits to each of their capital accounts were made at the end of 1942 and 1943 for taxes on income which was attributed to each one under bookkeeping entries made in their capital accounts. At the end of 1943 and 1944, each capital account of Albert and Betty was credited with one-sixteenth of the earnings for each year. At the end of 1943, the balance in each of the children's capital accounts was \$46,074.86.

During 1943 and 1944, the partnership, carrying on business under the name of Union Manufacturing Company, had two members only, Anna and Morris Harris. Albert and Betty Harris were not bona fide members of the partnership. There was no creation of a new and bona fide partnership of four members in 1943.

Personal income taxes for the year 1942 were paid to the State of California by Morris Harris in the amount of \$26,746.65, and by Anna Harris in the amount of \$25,256.18. Petitioners, in computing their victory tax liability for the year 1943, deducted the above amounts of California tax in their respective returns. Respondent disallowed each deduction in determining each petitioner's net income subject to 1943 victory tax.

OPINION

Harron, Judge: Anna and Morris Harris are co-partners in the partnership which conducts business as Union Manufacturing Company. The partnership, consisting of the petitioners, is not questioned by the Commissioner. [78] But respondent has determined that their son and daughter were not members of a co-partnership with petitioners, and he has taxed to petitioners income which was reported as the children's shares of the earnings of Union Manufacturing Company in 1943 and 1944. The question is whether one-sixteenth of the earnings of the above business is taxable to Albert Harris, and the same proportion to Betty Harris

as partners in Union Manufacturing Company, as petitioners contend; or whether such portions of the earnings are taxable to petitioners as part of the share of each one in the earnings of the partnership of which they are indisputably partners.

Admittedly, Albert and Betty Harris did not have capital of their own to contribute to a business venture as the contribution of partners. Petitioners allege that they made gifts of undivided one-sixteenth interests in a going business venture and that, thereupon, each child re-contributed what he is said to have received, namely, an undivided interest. Respondent does not admit that any completed gifts in praesenti were made to the children. It is pointed out that one issue presented by the pleadings is whether the alleged gifts were made. In amended petitions, each petitioner alleges, inter alia, that on January 2, 1943, he and she gave an undivided part of his and her interest to each one of the children. Respondent denies this pleading in his amended answer. It is necessary, therefore, to consider the question which is put in issue, namely, whether bona fide gifts in praesenti were made.

The petitioners contend that a partnership was created on January 1, 1943, in which each child was a co-partner, and that the partnership should be recognized for Federal income tax purposes. This question is put in issue by the pleadings of the petitioners that on January 2, 1943, the four members of the family agreed to associate them-

selves as co-partners, which [79] pleading the respondent has denied.

Petitioners state that they are familiar with the rule set forth in *Commissioner v. Tower*, 327 U. S. 280. They argue that the rule of that case, applied to the facts of this case, compel a holding that the alleged partnership of January 2, 1943, including the two children, must be recognized for Federal income tax purposes. Respondent argues that petitioners have misconstrued the rule of the *Tower* case. He cites the *Tower* case in support of his determination, and other cases where it has been applied, namely, *John G. Scherf*, 7 T. C. 346; *aff'd.*, 161 Fed. (2d) 495, certiorari denied, 68 S. Ct. 111; *M. M. Monroe*, 7 T. C. 278; *Jacob De Korse*, 5 T. C. 94; *aff'd.*, 158 Fed. (2d) 801; *W. M. Mauldin*, 5 T. C. 743; *aff'd.*, 155 Fed. (2d) 666; and *O. William Lowry et al.*, 3 T. C. 730; *aff'd.*, 154 Fed. (2d) 448, certiorari denied, 329 U. S. 725.

Petitioners are in no better position in this case than were the taxpayers in *John G. Scherf*, *supra*; *Jacob De Korse*, *supra*; and *W. M. Mauldin*, *supra*. Their contentions are not now, but have been considered, under similar facts, in many cases by this Court, and other courts. In other words, petitioners present a contention by which, in effect, they ask to have the underlying principles in this type of issue reviewed for them. We think it is unnecessary to do so, other than to point out that the question arises under section 22(a) of the Internal Revenue Code which broadly defines the

gross income which is to be taxed to an individual as including "gains or profits and income derived from any source whatever." The revenue acts do not recognize partnerships as taxable entities separate and apart from the individual partners, but provide that "Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity." [80] See section 181, Internal Revenue Code. And since the partners are liable for tax in their individual capacity, the broad scope of section 22(a) must be considered.

Here, as in the *Tower* case, and a line of cases which have followed in its path, two members of a family have undertaken to apportion their income among the members of the family group. In this case the arrangement purports to divide two tax units into four. The evidence fails to show that there was any intent that either one of the children would join with petitioners in "carrying on business in partnership" in the taxable years, (section 181, I.R.C.); or that there was any real change in the control over the income by the petitioners. Section 22(a) of the Internal Revenue Code is the corner stone of the Supreme Court's decision in the *Tower* case. Petitioners fail to understand that they have the burden of proving that something less than their respective 50 per cent shares of the income of an established business is taxable to them under sections 22(a) and 181, for they pass lightly over the matter of proving that bona fide gifts of interests were made, and of proving that

their two children were, in fact, carrying on a business with them in partnership. They miss the force of the phrase which appears at least twice in the opinion in the Tower case, which they even quote, to wit, that the issue turns on whether the junior members of the family and the senior members of the family "really intended to carry on business in partnership" in the taxable years, because they do not perceive that the Supreme Court clearly stated what factors should be shown as a matter of proof of such intent. The Supreme Court observed that: [81]

* * * A partnership is generally said to be created when persons join together their money, goods, labor, or skill for the purpose of carrying on a trade, * * * or business, and when there is a community of interest in the profits and losses. * * * A husband and wife [parent and child] may, under certain circumstances, become partners for tax, as for other, purposes. If she [the wife or child] either invests capital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, or does all of these things she may be a partner as contemplated by * * * 26 U.S.C.A. Int. Rev. Code, pars. 181, 182.

The contention that the daughter, Betty, was a partner in the Union Manufacturing business is

particularly without merit. There is no evidence that she desired to, or intended to, or did carry on the business enterprise in partnership with her parents in the taxable years. She was about seventeen years old in 1943; she had no capital of her own; and she performed no services in the business. There is no evidence of a completed transfer of an interest in the business to her such as would put in her complete dominion and control over an interest in the business and the earnings thereof, and such as would remove from the alleged donor—mother or father—whichever claims to have made the gift (the record on this point being confused)—control over his or her purported interest and share of earnings. See *Edson v. Lucas*, 40 Fed. (2d) 398, and cases cited therein. The evidence with respect to the alleged gift to Betty is merely that if a gift were made to the son, it would be fair to make a like gift to the daughter. Whichever petitioner alleges to have made this gift intended that the interest should be retained in the business as well as the earnings, nothing to the contrary having been shown by competent evidence. We are unable to find that a bona fide gift was made to Betty of a present interest in the business. We sustain the respondent's determination that one-sixteenth of the earnings [82] attributed to her is taxable to the alleged donor, either Anna or Morris Harris.

In support of their contention that the son, Albert, was a co-partner with them in their business

during 1943 and 1944, petitioners refer us to certain cases where it has been held, upon particular facts, that a father and son were co-partners. The holdings in such cases do not provide these petitioners authority in support of their contention. Such cases are distinguishable on their particular facts. Also, *Weizer v. Commissioner*, — Fed. (2d) — (C.C.A. 6), decided January 26, 1948, is inapposite, the facts being quite different.

Albert had an ambition to go into his father's business. He had done various things about the plant and office, without pay, during vacations and after school prior to 1943. But none of his activities, considering his youthful age and consequent limitations, had been sufficiently substantial to have taken him into any substantial or important work in the business before 1943. Cf. *John G. Scherf*, *supra*. In 1943 and 1944, his absence, therefore, was not absence from a business activity in which he had previously rooted himself. Therefore, little weight can be given his casual activities at his father's "shop" as a school boy, and full weight must be accorded the fact that he rendered no services whatsoever during 1943 and 1944. See *M. M. Monroe*, *supra*.

Albert contributed no capital to the Union Manufacturing Company business originating with himself. Furthermore, the evidence is not present to show that the purported gift to Albert of an interest in the business was a completed gift in *praesenti* which vested in him complete dominion

and control over an interest in and earnings of the business. *Edson v. Lucas*, *supra*. There was no written partnership agreement. The alleged verbal [83] agreement was a loose one. There is no evidence to clearly show that the usual terms of a partnership agreement were worked out so as to definitely establish the rights and duties of the son if he were to really carry on a business in partnership with his parents during the taxable years. The only inference which can be made from the record is that management of the business was to remain in Morris Harris, and that he was to continue to control the business and the earnings, as far as his children might be concerned. Partnership books were not closed. There were only bookkeeping entries which served to provide the basis for allocating earnings to the young son who was in school, at first, and later in the Army.

Upon consideration of all of the facts, we cannot find that Albert was a bona fide co-partner in the business in 1943 and 1944. Applying the rationale of the *Tower* case, we sustain respondent's determination. See *John G. Scherf*, *supra*.

The second question is whether state income taxes are deductible in computing victory tax net income.

Section 172(a) of the 1942 Revenue Act enacted a new tax called the victory tax which was to be levied upon income in years beginning after December 31, 1942. Section 172(a) of the 1942 Revenue Act added new provisions to the Internal

Revenue Code, sections 450 to 456. These provisions of the Internal Revenue Code provided for the computation of the new tax without reference to Chapter 1—Income Tax, of the Internal Revenue Code excepting where the statutory provisions relating to the computation of net income for the income tax were specifically made to apply by cross-reference. That is to say, the computation of the income tax and the computation of the victory tax are separate, the first being covered by [84] Subchapters A, B and C; and the second being covered by Subchapter D. For example, section 21 of the Internal Revenue Code (Subchapter B, Part 1) defines “net income” for purposes of the income tax; and section 451 of the Internal Revenue Code (Subchapter D—Part 1) defines “victory tax net income.” Also, the respective Subchapters make specific provisions for the various types of deductions which are allowable in computing “net income” and “victory tax net income.”

It must be kept in mind that all deductions are a matter of legislative grace. The question which is now raised by the petitioners under the victory tax net income provisions of the Internal Revenue Code must be considered upon the basis of the specific statutory provisions which allow deductions. Section 451(a)(3) states what taxes may be deducted in computing “victory tax net income.” The provision is as follows:

Section 451. Victory Tax Net Income.

(a) Definition.

* * * *

(3) Taxes—Amounts allowable as a deduction by section 23(c), to the extent such amounts are paid or incurred in connection with the carrying on of a trade or business, or in connection with property used in the trade or business, or in connection with property held for the production of income.

The subsection above quoted contains a limitation. First there is cross-reference to section 23(c) of the Internal Revenue Code which relates to the deduction of taxes generally for the purpose of computing "net income." Under section 23(c) there is the general provision that taxes paid or accrued within the taxable year are deductible, but the exceptions to the general rule are set forth. Income taxes paid to a state are not within the exceptions, and they are deductible in computing net income for the income tax [85]

However, the limitation contained in section 451 (a)(3) is that only those taxes which are deductible under section 23(c) which "are paid or incurred in connection with the carrying on of a trade or business, or in connection with the property used in the trade or business, or in connection with property held for the production of income" may be deducted for the purpose of computing the victory tax net income.

It is our understanding that the California income tax is a personal income tax which, like the Federal income tax, is imposed upon income de-

rived from all sources. Petitioners do not cite any cases which give contrary construction of the California statute. We do not have the personal income tax returns of the petitioners in evidence, neither the state nor the Federal returns. It is assumed that most of the income of the petitioners which was reported for both state and Federal income tax was derived chiefly from the partnership business. Petitioners argue that the state income tax was a tax which was paid or incurred in connection with the carrying on of a business within the meaning of section 451(a)(3) because the income which was taxed by the state was derived from a business.

The construction which the petitioners would have placed upon section 451(a)(3) does not, in our opinion, give proper consideration to the wording of the pertinent section. The state income tax was not incurred "in connection with the carrying on of the business." Those words have a clear meaning, but, if it is necessary to undertake to clarify them, we think that the words mean a tax which is incurred as an incident to the carrying on of business in the sense that a business expense is incurred in carrying on a business; that is to say, something which must be paid in order to do business. [86]

The specific question raised by petitioners is covered by a ruling of the Commissioner, I.T. 3644, which comes to the conclusion that "the personal income taxes imposed by the various states are not

deductible in whole or in part in computing victory tax net income under section 451(a)(3) of the Internal Revenue Code, *supra*." We think this ruling is correct and that the report of the Committee on Finance of the Senate, which accompanied the Revenue Bill of 1942, supports the Commissioner's ruling. See C.B. 1944, p. 373; Senate Report No. 1631, 77th Congress, 2d Session; C.B. 1942-2, 504, 509.

Petitioners think that the ruling set forth in I.T. 3644 may be in conflict with another ruling of the Commissioner, I.T. 3829, C.B. 1946-2, p. 38. The latter ruling was made in connection with the deductions allowed for the purposes of computing adjusted gross income under section 22(n)(1) of the Internal Revenue Code. That section relates to the income tax. We think that the ruling made under I.T. 3829 does not apply in making an interpretation of section 451(a)(3) which relates to the computation of victory tax net income. It has been noted before that state income taxes are deductible for the purpose of computing the income tax, and the ruling in I.T. 3829 is consistent with the statutory allowance of deduction for state income tax. The crux of the matter is that the Congress did not see fit to permit deduction of state income taxes in the computation of the [87] victory tax net income for the purpose of the victory tax.¹

¹ See Senate Report No. 1631, 77th Congress, 2d Session; C.B. 1942-2, p. 509, where the following is stated:

Since the victory tax does not allow any deduc-

We think that this is a complete answer to the petitioner's contention.

Reviewed by the Court.

Decisions will be entered for the respondent. [88]

The Tax Court of the United States
Washington

Docket No. 12984

ANNA HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, promulgated on May 12, 1948, it is

Ordered and Decided: That there are deficiencies in Federal income and victory tax for the years 1943 and 1944 in the respective amounts of \$5,-662.73 and \$18,136.67.

Enter May 12, 1948.

(Seal) /s/ MARION J. HARRON,
Judge.

[89]

tion for state income taxes your Committee deemed it advisable to provide that the total income tax and victory tax should not exceed 90% of the taxpayer's net income * * *.

The Tax Court of the United States
Washington

Docket No. 12985

MORRIS HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, promulgated on May 12, 1948, it is

Ordered and Decided: That there are deficiencies in income and victory tax for the years 1943 and 1944 in the respective amounts of \$6,035.87 and \$18,693.10.

Enter May 12, 1948.

(Seal) /s/ MARION J. HARRON,
Judge.

[90]

The Tax Court of the United States

Docket No. 12984

ANNA HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Docket No. 12985

MORRIS HARRIS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Court Room No. 229,

United States Post Office and Court House Bldg.,

Los Angeles, California

January 29, 1948—9:30 a.m.

(Met pursuant to notice.)

Before: Honorable Marion J. Harron, Judge.

Appearances: D. Webster Egan, 403 West 8th Street, Los Angeles, California, appearing for the Petitioner. Dana Latham, 411 West 5th Street, Los Angeles, California, appearing for the Petitioner. [92] T. M. Mather. (Honorable Charles Oliphant, Chief Counsel, Bureau of Internal Revenue), appearing for the Respondent. [93]

PROCEEDINGS

The Court: Docket Nos. 12984 and 12985, Anna Harris and Morris Harris. Will counsel please state appearances for the record.

Mr. Egan: D. Webster Egan. Your, Honor, the Petitioner wishes to add the name of Mr. Dana Latham, as associate counsel.

Mr. Mather: Mr. Mather, for the Respondent.

The Court: Proceed, Mr. Egan.

Mr. Egan: Your Honor, these deficiencies, most of them at least, come about by reason of the following: That on or about January 1st or 2nd, 1943, the Petitioners filed herein were co-partners in a manufacturing company, co-partnership. About that time they transferred, each to two minor children, an undivided sixteenth interest in and to the property and assets of the co-partnership. We believe that the evidence will show that there was no restrictions whatsoever on these gifts and further that there was no charges made against the minor's accounts for support, maintenance or education.

The other issue in the case concerns the question of charging to expense, in the year 1943 on petition of Morris Harris' return, the sum of \$26,747.65. as a deduction for the purpose of computing the victory tax. In the case of Anna Harris, her charge was \$25,256.18, as a deduction against the computing of the victory tax, these two amounts being income [96] taxes paid to the State of California. We believe that these two amounts are proper charges against the business income of both of these Petitioners.

Mr. Mather: If your Honor please, at this time I would like to move that the cases be consolidated.

The Court: Motion granted.

Mr. Mather: As stated by counsel for the Petitioner, those are the two issues. Under the pleadings, there is no issue with respect to any partnership; merely the validity of a gift by the partners, these Petitioners, to their children of a one-sixteenth interest in their business.

The petition alleges that the Petitioners were partners, operating under the firm name of Union Manufacturing Company, and that allegation is admitted. It also alleges that they made a gift to their children of a one-sixteenth interest, and that is denied.

With respect to the other issue, the deduction of state income taxes in determining the victory tax net income, the position of the Respondent is that there is no statutory provision allowing that deduction, and that the legislative history of Section 451, of the Code, specifically precludes the deduction.

Mr. Latham: If your Honor please, I don't know what Mr. Mather had in mind regarding his statement that there was no issue with respect to the validity of this partnership for [97] tax purposes. The petition recites that the Respondent proposes to add the taxpayer's net income for the year 1944, and also a different amount for year 1943, a certain amount being the amount of the income of certain of the children, and recited as having been received by the children from their interest in the partnership.

Now, it is true that there is no specific statement in the statement of facts, to the effect that these people were partners, but that at best would be merely a conclusion of law, it seems to me.

The Court: I think Mr. Mather means, we do not have in this case the question of whether Morris Harris and his wife, Anna Harris, carried on a business in partnership, under the name of Union Manufacturing Company.

Mr. Latham: There is no issue with respect to that point.

The Court: That issue has been raised in a good many cases and Mr. Mather just wanted to point out that we do not have that issue in this case.

Mr. Latham: That is what I had in mind. Might I say this, your Honor—

The Court: Let me finish. We had a history of cases, as you know, where the taxpayer, husband or wife, carried on a business with them in partnership. In this case the Respondent has not determined that Anna Harris is not a member of a [98] bona fide partnership. He did not determine that. You, in your petition, allege perhaps that there was a partnership, but whether you did or didn't, there is not a question about the property right of Anna Harris reporting, at least, or at the most, one half of the net income of the Union Manufacturing Company.

Now, you have come to the matter of a husband and wife, who carry on a business in partnership and either or both give an undivided interest to a child. Now, do you mean that you would understand that to raise a question of whether the child

was a member of the partnership, that could be a question in the case?

Mr. Latham: That is my understanding of Mr. Mather's point.

The Court: Supposing you state your contention, please, the Petitioners' theory and let Mr. Mather worry about the Respondent's theory.

Mr. Latham: The Petitioners' theory is that the gift of an interest in the assets of a going partnership, was made to each of the children, and at the same time, a partnership was created, in which the children were partners.

The Court: That would be a matter you would have to prove.

Mr. Latham: That is correct.

The Court: Were there one or more children?

Mr. Latham: Two.

The Court: What were their names?

Mr. Latham: Albert P. and Betty.

The Court: Do the Petitioners contend that each was given a one-sixteenth, or both?

Mr. Latham: Each.

The Court: What do you intend to show as to the making of gifts; who made these gifts?

Mr. Latham: One parent made a gift to one child and the other to the other.

The Court: Who did it?

Mr. Latham: Mr. Harris made a gift to his daughter, Betty, and Mrs. Harris made a gift to her son, Albert.

The Court: All right. What else does the Petitioner intend to show?

Mr. Latham: We intend to show participation in the activities of the partnership by the son and show the circumstances leading up to the formation of the partnership.

The Court: Now, are you contending that the partnership consisted of four people, or that the partnership consisted of two?

Mr. Latham: That the partnership consisted of four people.

The Court: That is the Petitioners' contention.

Mr. Latham: That is the Petitioners' contention. [100]

Now, there has never been any question but what a partnership existed between Mr. and Mrs. Harris.

The Court: That is my understanding. The issue in the case is, whether a partnership existed among Mr. & Mrs. Harris and Albert and Betty Harris.

Mr. Latham: That is correct.

Mr. Mather: That is correct, your Honor, but there is no allegation that the children were partners in the pleadings.

The Court: I see.

Mr. Egan: If your Honor please, the facts allege that each child received an undivided one-sixteenth interest in and to the assets of Union Manufacturing Company, which is a co-partnership. Now, to allege they were partners, would simply be a conclusion of law.

The Court: Well, perhaps not where you have a tax question, Mr. Egan.

Mr. Egan: Well, the Commissioner is pretty

technical on some of these things. As a matter of pleadings, it would be a conclusion of law.

The Court: This is a specialized field that we work in, and that is a technical point, but I would be inclined to agree with Mr. Mather, that the pleadings ought to cover that. You should not rest on the fact of the transfer of the interest in and of itself. [101]

Mr. Egan: Don't you think that is a matter of evidence? As I say, if I were to allege they were co-partners, it would be simply a conclusion of law.

The Court: I do not think so, because the issue for tax purposes, whether you have a partnership relation so that the income of a business or property is taxable to various people, which you contend are partners, is a particular kind of issue that requires the introduction of particular evidence. I think your pleadings will be clearer if you set forth that you contend the children were members of the partnership. We will assume that that is what your pleading means, and I think we do not need to spend any more time discussing this particular matter.

Mr. Latham: May we have leave to file amended petitions within ten days?

The Court: Certainly. It is all right to have the question raised. If there is any doubt about the pleadings, the question should be raised at the trial.

Mr. Mather: If your Honor please, I have no objection to such amendment. I would like to

state, in connection therewith, that the evidence will show that these gifts, if they were gifts, emanated from the parents to their children, and there was no contribution of capital by the children, emanating from themselves, to any partnership; that it is the position of the Respondent, that the evidence will show that the [102] children were minors at the time, and that no services were performed by the children.

The Court: Are you ready to proceed?

Mr. Latham: Yes, your Honor. By agreement with Mr. Mather, subject to your approval, and in the interest of speeding this case, we will be a little informal on introduction of certain documents and evidence.

With respect to issue number one, namely the deductibility of the California State income tax, in determining victory tax net income for the year 1943, I offer in evidence this docket, 12984, as Petitioners' Exhibit No. 1, a retained copy of Morris Harris' 1942 California State income tax return.

Mr. Mather: No objection.

Mr. Latham: This shows a tax due of \$26,746.65, and I believe it may be stipulated that that amount was paid by Mr. Harris to the State of California, during the calendar year 1943.

Mr. Mather: I think it is admitted in the pleadings.

The Court: Received as Petitioners' Exhibit 1.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 1.)

[Petitioners' Exhibit No. 1 is set out in full, page 130, of this printed Record.]

The Court: Since the cases are consolidated, you do not have to refer to the docket number.

Mr. Latham: That only applies to Morris Harris. All the other evidence will apply to both cases?

The Court: No. When your cases are consolidated your evidence applies to the consolidated proceedings, and you are just wasting time referring to the different dockets.

Mr. Latham: All right. As Petitioners' Exhibit No. 2, the retained California State income tax return of Anna Harris for the calendar year 1942, showing a tax of \$25,256.18, which may be stipulated was paid to the State of California during the calendar year 1943.

Mr. Mather: No objection.

The Court: Received as Exhibit 2.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 2.)

[Petitioners' Exhibit No. 2 is set out in full, page 134, of this printed Record.]

Mr. Latham: Mrs. Harris, take the stand, please. Whereupon,

ANNA HARRIS,

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: State your name, please.

The Witness: Anna Harris.

(Testimony of Anna Harris.)

Direct Examination

By Mr. Latham:

Q. Will you state your name for the record, please? A. Anna Harris.

Q. Your address? [104]

A. 13098 Sunset Boulevard, Los Angeles.

Q. You are one of the Petitioners in this proceeding? A. Yes.

Q. Are you connected with the Union Manufacturing Company of Los Angeles? A. Yes.

Q. In what capacity? A. A partner.

Q. State briefly, for the Court, your connection with that concern, from the beginning to the present, very briefly.

A. Well, the partnership was formed in 1909 and I used to go there to work after school. I attended high school at that time and continued until I finished high school and after that I put in my full time.

Q. Who were the partners in 1909?

A. Mr. Harris and my father, Mr. Pinkert.

Q. By Mr. Harris you mean your husband?

A. Well, my husband now.

Q. Proceed.

A. Then, after I finished high school, I continued and put in my time, and in 1919 Mr. Harris and I were married. I continued right in the business, doing practically everything outside of manufacturing the materials that were manufactured. I took care of the credits in the office, the book-keeping, the correspondence, waited on the trade

(Testimony of Anna Harris.)

who came into the place and, [105] well, just about did everything, for my father and Mr. Harris.

Q. State the nature of the business of the partnership.

A. It is a manufacturing business of work and outing clothing.

Q. Has it been that type of business during the entire period?

A. Yes, but it grew and grew and as it grew, we engaged bookkeepers, stenographers and what not. My capacity was much more executive then. With all the work, plus bookkeeping, very often I was so busy I had to take my bookkeeping home. I worked day and night, practically, before that. My father took care of the outside selling and my husband took care of the inside manufacturing. I did all the rest. That is the way we worked until practically up to date. I am not active now, but I was for many, many years.

Q. How long did the partnership between your husband and your father continue?

A. Until '23, I believe. Until the end of '23; about 14 years.

Q. Then what happened?

A. My father stepped out and I became a partner. My father retired.

Mr. Latham: I offer as Petitioners' Exhibit 3, photostatic copy of a partnership agreement between Morris Harris and the witness, Anna Harris, dated January 2, 1924. [106]

Mr. Mather: No objection.

The Court: That will be marked and referred

(Testimony of Anna Harris.)

to as Petitioners' Exhibit 3. Received in evidence.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 3.)

[Petitioners' Exhibit No. 3 is set out in full, page 137, of this printed Record.]

By Mr. Latham:

Q. Mrs. Harris, I show you this document and ask you if you know what it is.

A. Yes, that is our partnership agreement.

Q. That partnership agreement, between your husband and yourself, actually was executed on the date it bears?

A. Yes, that is right.

Q. Did you continue to give your full time, or practically full time, to the affairs of the partnership after January, 1924?

A. Well, not my full time, but a great deal of the time, because I had a child at that time. I kept in very close touch to it and gave a good deal of my time, but not as much as I did before.

Q. You actually went directly to the office of the company?

A. Oh, yes, I did and gave a lot of time to it.

Q. Did you perform the same general type of services that you performed prior to 1924?

A. Yes. [107]

Q. You have two children? A. Yes.

Q. Will you state their names and ages, birth dates?

A. Albert Harris, born June 14, 1923 and Betty Harris, born September 22, 1926.

(Testimony of Anna Harris.)

Q. Your son, Albert, is in the courtroom?

A. That is right.

Q. I show you another document, purporting to bear on its face, the date, April 1, 1937, and ask you to state what it is.

A. I imagine that is a renewal of the partnership between myself and Mr. Harris.

Q. In other words, the first agreement of 1924, provided for a ten-year term?

A. That is right, and that is the renewal.

Q. Was this signed at the suggestion of your then attorney? A. That is right.

Mr. Latham: I will offer in evidence, as Petitioners' Exhibit No. 4, photostatic copy of partnership agreement between Morris Harris and Anna Harris, dated April 1, 1937.

Mr. Mather: No objection.

The Court: Received as Exhibit 4.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 4.) [108]

By Mr. Latham:

Q. How long did you continue to operate under this second partnership agreement between yourself and your husband?

A. Well, until we made the change—you mean taking in the children?

Q. Yes. A. Until January, 1943.

Q. Now, please state the events leading up to

(Testimony of Anna Harris.)

this change in 1943, which you have just referred to.

A. Well, along about 1937, it seemed we noticed an interest in Albert to join our business. Of course, he was just a little fellow of about 14, but Mr. Harris had received a letter from someone offering to buy our business, and he was more or less interested in selling it because he thought we would like to retire, but Albert was very much opposed to that and said he had always hoped to go into this business with his father, when he was old enough. So, for that reason, Mr. Harris gave up the idea of ever selling it and waited until such time as Albert would be old enough to join him. But when he graduated from high school he didn't want to go to college. He wanted to go into the business. We wanted him to have more education—

Q. When did he graduate from high school?

A. In '40 or '41. I don't remember exactly, but we prevailed upon him to continue and go to college, because we felt [109] he would be worth more to the business if he had more education.

Then he came home from college; he went to the University of Virginia, that summer.

Q. Just when did he enter the University of Virginia?

A. Must have entered it in the fall of '40, '41, I think, but he came home.

Q. What kind of a course was he taking?

A. Just a general educational course, and when he came back, that summer—

(Testimony of Anna Harris.)

Q. Now, that is the summer of '42?

A. '42. He worked in the factory in all the various departments. He seemed to be very interested, sort of just taking it all in. He made up his mind then and there that that was the thing he would rather do, than even go to school, so that summer he took a night course at U.S.C., on textiles. Then, we prevailed upon him to go back to college. He changed colleges because the University of Virginia didn't offer the course that would be suitable for his training in textiles, and he went to the State University of North or South Carolina—Raleigh—because that school offered the course that was suitable for his business.

We then decided that he would follow that, and just by way of inducement, we wanted to give him a small interest in the business. We talked it over then and decided that was [110] the way it would be.

Q. Did you then give him this sixteenth interest in the partnership assets, of which you were a partner, pursuant to the statement that has been made heretofore?

A. Well, we did, beginning in 1943, beginning in January. That is the way we thought it would be a good idea to do.

Q. With whom was that gift and the formation of the new partnership discussed?

A. Well, we discussed it with Albert before he went back to school, and then he came back at Christmas time and we discussed it some more, be-

(Testimony of Anna Harris.)

cause I think we had seen Mr. Egan about it, to see just how we could do it.

Q. Your attorney? A. Yes.

Q. Was it also discussed with Mr. Harris and with Betty?

A. Oh, yes, we all discussed it, yes.

Q. So that— A. We also—pardon me.

Q. Go ahead.

A. We also felt that as long as we were giving Albert a small share, just having the two children, we felt it would be fair to give Betty the same share, and although she was very young, she always showed an interest. We felt that after her college, if she wasn't married, she would step in.

Q. She had not and did not work in the business as Albert did?

A. No, but she showed an interest.

Q. Is it a fair statement, that Christmas of 1942, before Albert returned to college, it was clearly understood between the four of you, that this partnership was to go into effect as of the 1st of January, 1943? A. Yes.

Q. Was there ever any writing, evidencing this new partnership?

A. What do you mean by that?

Q. Was it ever reduced to writing, such as was the case in the prior partnership?

A. Yes, it was. Later in the year; we didn't do it right away.

Q. Now, you never did have an actual agreement? A. No, we had no agreement.

Q. That is, in writing, I mean. A. No.

(Testimony of Anna Harris.)

Q. Why was that?

A. Well, I guess because we are just lax about those things. We felt that as long as we had decided to have the partnership, that that was all there was to it; that, actually, if we gave them that share, it was a partnership. We just neglected to do it. [112]

Q. Isn't it a fact, that Mr. Egan advised you that a writing was not necessary, a written agreement was not necessary?

A. I don't remember, excepting that I assumed that. Yes, I think that is the way we thought it should be done.

Q. Now, in connection with this oral agreement between the four of you, was there any restrictions between you with respect to the rights of the children, either as to activities or withdrawals from the partnership? A. No, none at all.

The Court: Are you offering in evidence any written agreement of the partnership?

Mr. Latham: There was none, your Honor, with respect to this particular partnership, upon the advice of Mr. Egan, whom we will put on the stand if necessary.

The Witness: That is right.

By Mr. Latham:

Q. Now, what kind of work—

The Court: Excuse me, please. What evidence of partnership was there?

Mr. Latham: The understanding of the parties, followed by the appropriate book entries, which will

(Testimony of Anna Harris.)

be offered in evidence, the filing of partnership tax returns and so forth and then there also—

The Court: Was that an oral arrangement?

Mr. Latham: This one was an oral arrangement, and confirmed in writing later by a subsequent partnership agreement, which my office drew in 1947, when the interest of the parties were changed, due to the purchase of Albert of a small additional interest in 1946.

The Witness: That is right.

Mr. Latham: Now, that interest in 1946, is not here involved because we are only dealing with the years 1943 and 1944, but we did suggest to Mr. and Mrs. Harris and Albert, that the present understanding, or the one that had been in effect since 1943, should be reduced to writing, which was done.

The Court: What evidence of a gift was there?

Mr. Latham: We have the gift tax return, which we propose to offer in evidence.

The Court: That is the only evidence of a gift?

Mr. Latham: Well, plus the book entries. I don't know what other evidence is possible. The statement of the partners—I can't think of any other evidence that would be available, under any circumstances.

The Court: There could be. I just was inquiring. All right. Go ahead.

By Mr. Latham:

Q. You say, that Albert worked throughout the summer of 1942 at the plant? [114]

A. That is right.

Q. In various departments of the business?

(Testimony of Anna Harris.)

A. Yes, all around; making a general survey of everything.

Q. Becoming familiar with the operation of the business? A. That is right.

The Court: Well, now, how long a period would that be, Mrs. Harris?

The Witness: Well, I don't know just when he got out of school, but it would be until the following term. I imagine it was June.

The Court: College vacation usually runs for about two and a half months?

The Witness: About three months, June, July and August. Something like that.

The Court: All right.

By Mr. Latham:

Q. Prior to the summer of 1942, had Albert done any work in the business?

A. Yes, he worked after school, when he went to high school, and on Saturdays.

Q. And a portion of the summer vacation?

A. Yes.

Q. During the summer of 1942, did Albert draw any salary [115] or pay from the business?

A. No, he didn't.

Q. Will you state to the court why he did not?

A. Well, because it would entail a social security number and a lot of other things that are important when people work, and we felt it was unnecessary for him because eventually we felt it would be a partnership and he wouldn't need it, also he really didn't need the money; we took care of him. We

(Testimony of Anna Harris.)

felt too that perhaps the employees wouldn't think it was right, that as long as there was work to be done, that perhaps someone who needed the money more than he did should have it.

So, we didn't pay him anything.

Q. Now, what happened when Albert returned to the textile school at North Carolina? After the Christmas vacation of 1942.

A. Well, he enlisted very soon afterward in the E.R.C.; in December, I think, of that year. He felt he would be called very soon, and he preferred to enlist, rather than be drafted.

Q. When was he called into service?

A. April of the following year; the following April, I would say.

Q. April of 1943? A. That is right.

Q. When did he return from the service?

A. In July, 1945—no, not from the service, he returned in January, 1946. [115]

Q. He was discharged at that time?

A. He was not discharged then, but he came back from overseas in July, 1945.

Q. What did he do immediately upon his discharge?

A. He started to work immediately. We thought he should have a little vacation, but he went to work.

Q. Right to work in the business?

A. That is right.

Q. Has he worked continuously in the business from that time to the present?

(Testimony of Anna Harris.)

A. Yes. He has never had any time off either.

Q. In what capacity?

A. Well, in the general capacity, executive. He is a great help to Mr. Harris in every way. All the things he would do, he is letting drop off on Albert, because he needs that help.

Mr. Latham: Will it be stipulated that appropriate Federal partnership returns were filed for the years in question, in which the four individuals here mentioned, were named as partners?

Mr. Mather: Well, no, I couldn't stipulate that appropriate returns were filed, Mr. Latham.

Mr. Latham: Shall we say, the Form 1065?

Mr. Mather: Partnership returns were filed for the partnership, in which, for 1943 and 1944, in which a [117] distributive share of the partnership income is shown as being allocated to the children, and that the children filed, or I should say, that returns were filed for the children, signed by their mother, for 1942 and 1943.

Mr. Latham: 1943 and 1944.

Mr. Mather: Yes.

Mr. Latham: I am not asking you to stipulate that they are partners, I am just asking you to agree that the Form 1065, which is the Federal partnership return, was filed for the years 1943 and 1944, in which Albert and Betty Harris were shown as receiving one-sixteenth interest in the partnership income.

Mr. Mather: They were shown as—

The Court: I think we had better have the re-

(Testimony of Anna Harris.)

turns in evidence, Mr. Mather. Do you want to offer them?

Mr. Latham: I would like to offer them. I will offer in evidence as—

The Court: Will you offer them, Mr. Mather, so they could be photostated in Washington?

Mr. Mather: I will request they be withdrawn and have photostats made.

The Court: You make that request.

Mr. Mather: I don't care to offer them myself.

Mr. Latham: I offer as Petitioners' Exhibit, I believe, No. 5 and 6, original partnership returns for the [118] calendar year 1943 and 1944, of the Union Manufacturing Company, 5S 1943 and 6S 1944.

Mr. Mather: No objection, your Honor. I would like to have the record show that those original partnership returns were produced from the Government file, and ask leave to withdraw them for substitute photostats.

The Court: That may be done. The returns are received as Exhibits 5 and 6.

(The documents above-referred to were received in evidence and marked Petitioners' Exhibits 5 and 6.)

[Petitioners' Exhibits No. 5 and 6 are set out in full, pages 139, 143, of this printed Record.]

Mr. Latham: I offer as Petitioners' Exhibit 7, a gift tax return, Form 709, by Anna Harris, covering the year 1943.

Mr. Mather: No objection.

The Court: Received as Exhibit No. 7.

(Testimony of Anna Harris.)

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 7.)

[Petitioners' Exhibit No. 7 is set out in full, page 149, of this printed Record.]

Mr. Latham: As Petitioners' Exhibit 8, donee's gift tax return by Albert P. Harris and that is Form 710.

The Court: Is his name Albert, A-L-B-E-R-T or E-L-B-E-R-T?

Mr. Latham: Albert—for the year 1943.

The Court: Received as Exhibit 8.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 8.)

[Petitioners' Exhibit No. 8 is set out in full, page 151, of this printed Record.]

Mr. Latham: As Petitioners' Exhibit 9, gift tax return for the year 1943, Form 709, of Morris Harris.

Mr. Mather: No objection.

The Court: Received as Exhibit 9.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 9.)

[Petitioners' Exhibit No. 9, see page 152, of this printed Record.]

Mr. Latham: As Exhibit 10, donee's gift tax return, for the year 1943, Betty Harris, donee, Form 710.

Mr. Mather: No objection.

The Court: Received as Exhibit No. 10.

(Testimony of Anna Harris.)

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 10.)

[Petitioners' Exhibit No. 10, see page 152 of this printed Record.]

Mr. Latham: And as Petitioners' Exhibit No. 11, photostatic copy of a Treasury Department letter, dated September 25, 1945 referring to the various gift tax returns just mentioned, increasing the valuation named and proposing an additional gift tax.

Mr. Mather: That is objected to as irrelevant and immaterial.

Mr. Latham: I think it is pertinent. It shows that the Treasury Department did recognize and act upon these various gift tax returns which we have just referred to.

The Court: Received as Exhibit 11.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 11.)

[Petitioners' Exhibit No. 11 is set out in full, page 152, of this printed Record.]

The Court: May I say, Mr. Latham, that we have held frequently that the termination of deficiency in a gift tax, is not material in determining the taxability of income in business.

Mr. Latham: I am fully familiar with that, your Honor. I simply make the observation as to what evidence we have that a gift, in fact, has been made. This is merely adding to that point.

(Testimony of Anna Harris.)

The Court: Mr. Egan's point, which he raised at the beginning, goes right to the heart of this issue.

Mr. Latham: We make no contention—

The Court: You see, you can make a gift. You can do a great many things that you want to do, but whether or not that will alter the relations and income, if I may put it that way, is the question that is involved in this case.

Mr. Latham: As a matter of fact, if I understand you, Mr. Mather, you conceded that the gift was, in fact, made, do you not?

Mr. Mather: No, I do not.

Mr. Latham: I think your answer concedes it.

Mr. Mather: I don't believe so. It specifically denies it.

Mr. Latham: All right.

By Mr. Latham:

Q. Mrs. Harris, I show you another document and ask you [121] to state what it is.

A. Yes. This is the partnership of all of us, after Betty and Albert were included.

Q. What is the date of this document?

A. May 20, 1947.

Q. Will you please state the circumstances—does that document bear your signature?

A. Yes, it does.

Q. Are those the signatures of Morris, Betty and Albert? A. Yes. All of them.

Q. Will you please state the circumstances under which the document was prepared and executed?

(Testimony of Anna Harris.)

A. Well, I consulted your office about some of our affairs and in the course of the conversation, you found out that we had no partnership agreement with the children. You thought it was necessary to have it. We didn't think it was and didn't have it.

Q. You mean, no partnership agreement in writing?

A. A written partnership agreement, yes.

Q. My office suggested your oral agreement be reduced to writing?

A. That is right, and you drew it up for us.

Mr. Latham: I will offer in evidence as Petitioners' Exhibit 12, the document which has been identified by this witness and which is dated May 20, 1947. [122]

Mr. Mather: That is objected to as irrelevant and immaterial. Taxable years are 1943 and 1944 and any arrangement that they might have had in subsequent years, would have no bearing on the issues involved in this proceeding.

The Court: Ojection sustained.

Mr. Latham: Could I be heard on that, if your Honor please?

The Court: Surely.

Mr. Latham: These partnership cases, as I understand it—the Government takes the position that the entire record should be looked at, in order to determine the intent of the parties; what actually happened and that sort of thing. Some question has been raised, I think, by your Honor, as to what

(Testimony of Anna Harris.)

evidence we had and while this, at best, may be deemed self-serving, it does seem to me a part of the complete picture just as the original partnership agreement, back in 1924. That, technically speaking, could have been objected to but was not, as being too early. It seems to me the relations of these parties, from the beginning to the present are all pertinent in determining whether or not a true partnership existed.

The Court: Mr. Latham, in these cases, the standard to be applied has now been settled by the Supreme Court, and under the rules, the evidence to be introduced must relate to the taxable year involved, or the preceding years. Now, [123] it has been testified by Mr. Harris that there was an agreement drawn up subsequently, and that is sufficient. It is not material to the year 1943, to have the agreement in evidence; terms of the agreement or anything else.

Mr. Latham: In the interest of speed, we will be just a little bit informal, if we may, your Honor please.

The Court: Well, don't hurry. I was hearing a case but I put it over now until 2:30 this afternoon. You have all the time you want.

Mr. Latham: I offer as Petitioners' Exhibits 12 and 13, original pages from the ledger of the Union Manufacturing Company, showing the capital accounts of Albert Harris and Betty Harris, the account of Albert Harris being No. 93 and that of Betty Harris No. 94, with the request, if your

(Testimony of Anna Harris.)

Honor please, that I may be permitted to substitute photostats for these originals.

The Court: I think all the capital accounts should be introduced.

Mr. Latham: I will be glad to. I have all four here.

The Court: You may withdraw and substitute photostats.

Mr. Latham: Then, Exhibit No. 14 will be the capital accounts.

The Court: It is very much better for you to offer [124] each page and say what it is. It shows up in the record, and it is easier for the court.

Mr. Latham: No. 12 will be, then—

The Court: Will be the next one.

Mr. Latham: The capital account of Morris Harris, one of the Petitioners, account No. 91.

The Court: Received as Exhibit 12.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 12.)

[Petitioners' Exhibit No. 12 is set out in full, page 154, of this printed Record.]

Mr. Latham: And as Exhibit 13, capital account of Anna Harris, account No. 92.

The Court: Received as Exhibit 13.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 13.)

[Petitioners' Exhibit No. 13 is set out in full, page 155, of this printed Record.]

(Testimony of Anna Harris.)

Mr. Latham: No. 14, that of Albert Harris, account No. 93.

The Court: Received as Exhibit No. 14.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 14.)

[Petitioners' Exhibit No. 14 is set out in full, page 156, of this printed Record.]

Mr. Latham: Exhibit 15, account No. 94, Betty Harris.

The Court: Received.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 15.)

[Petitioners' Exhibit No. 15 is set out in full, page 157, of this printed Record.]

Mr. Latham: I might state, that these began in 1942 [125] so far as Mr. and Mrs. Harris are concerned, and 1942 as far as the children are concerned. There will be no occasion to go back of those dates.

The Court: Are you going to ask the bookkeeper or an accountant to testify?

Mr. Latham: Not unless Mr. Mather or the Court desires. We have the bookkeeper here.

I would also like the record to show that I hold in my hand, the Union Manufacturing Company's general journal. There appears on page 40—

The Court: What are you going to do; are you going to read into the record the entries?

Mr. Latham: One entry, if your Honor please, which Mr. Mather is interested in.

(Testimony of Anna Harris.)

The Court: I think you should ask the accountant to testify.

Mr. Latham: Then, I may ask Mrs. Harris to step down and put the bookkeeper on the stand?

The Court: I don't think that is necessary. You can have your accountant come in later.

Mr. Mather: This is just one item in the journal which if Mr. Latham won't offer, I will have to.

The Court: Will you stipulate?

Mr. Mather: I will be very happy to.

Mr. Latham: We will stipulate that on page 40 of the [126] general journal, the following shows:

"1943: September 16, 1943, 1/1/43, M. Harris, Capital account, page 91, \$34,083.70."

Immediately below that:

"A Harris, Capital account No. 92, \$34,083.70."

Below that:

"Albert Harris, Capital account No. 93, \$34,083.70."

And below that:

"Betty Harris, Capital account No. 94, \$34,083.70," with the statement: "To transfer above interest in company to Albert and Betty Harris, son and daughter, one-sixteenth each, based on M. Harris' interest, \$270,049.36 and A. Harris' interest, \$275,289.73."

Then, those figures are added together, making a total of \$545,339.09. That completes the entry just stipulated.

The Court: What is that total figure?

Mr. Latham: Total of two prior capital accounts of Mr. and Mrs. Harris.

(Testimony of Anna Harris.)

The Court: That is page 40 of the general ledger?

Mr. Latham: Page 40, general ledger. I might state, there is only one reason for offering it at all.

The Court: There is no reason to show it to me. It is the record it has to get in.

Mr. Latham: It is the fact of the reference to 9-16-43 as of January 1, 1943. I think that is the only reason [127] that Mr. Mather is interested in that entry, and asked to have it introduced.

By Mr. Latham:

Q. Mrs. Harris, you have just heard me read the entry on page 40 of the general journal, of the Union Manufacturing Company. Do you know why that entry was not made until, apparently, September of 1943?

A. Well, I guess it was just an oversight because Mr. Egan probably thought that Mr. Harris would attend to it and Mr. Harris probably thought that Mr. Egan would tell Miss Goodenough, our bookkeeper, just how it should be done and it was neglected, as the time went along. In the course of conversation, we discovered that it hadn't been done. Mr. Egan very often would phone Miss Goodenough to tell her just how to do it. Mr. Harris assumed he had and he thought Mr. Harris had.

Q. Now, Mrs. Harris, the gifts that you have mentioned as made by yourself and your husband to your children, was not in fact made on or about September 16, 1943?

A. No.

Q. When was it made?

A. January.

Q. 1943?

A. Yes.

(Testimony of Anna Harris.)

Q. When was the understanding or oral agreement you referred to as to the new partnership reached between the four of [128] you?

A. Well, in December, just before January.

Q. To become effective the first of the following year?

A. Yes, become effective the first of the following year.

The Court: December what year?

The Witness: 1942. We decided on it to become effective 1943.

Mr. Latham: That is all.

Cross Examination

By Mr. Mather:

Q. Mrs. Harris, you were familiar with the conduct of the business from its inception, were you not? A. Yes.

The Court: We will take a short recess at that time.

(Short recess taken.)

The Court: Proceed.

By Mr. Mather:

Q. I believe I asked you if you were familiar with the conduct of the business over this period of years? A. Yes, I am.

Q. It is engaged in the manufacture of work clothes? A. That is right.

Q. Was there any change in the method in which the business was conducted, during the years that we are interested in? [129]

A. With respect to what—change of—

Q. The conduct of the business. Was it oper-

(Testimony of Anna Harris.)

ated the same in 1942, 1943, 1944 and 1945, as it always had been?

A. Yes, I guess so, excepting the change in partnership.

Q. Well, would that involve any change in the operation of the business or the conduct of the business?

A. We still manufacture the same things. I don't know just what you are referring to.

Q. Did it in the same way as you always had?

A. Yes.

Q. Neither of the children performed any service in 1942 and 1943, did they?

A. No, excepting—well, Albert worked in—in '42 did you say?

Q. '43 and '44.

A. '43 and '44. Well, Albert was in the Service, I think at that time. He couldn't very well. He would have—

Q. He entered North Carolina State Textile Engineering School in September, 1942 and then entered the Service April, 1943?

A. That is right.

Q. Now, no documents of any character were executed in connection with these gifts to the children other than the exhibits that have been offered here in evidence, is that [130] correct?

A. No documents, no. But we had oral agreements.

Q. No bill of sale or anything of that character?

A. No.

(Testimony of Anna Harris.)

Q. Did you have anything to do with separation of income tax returns? A. Yes.

Q. When the children were taken into the business, was the tax liability discussed?

A. I can't remember.

Q. There was no discussion, then, I understand?

A. No, I don't think so.

Mr. Mather: That is all.

Mr. Latham: That is all, Mrs. Harris.

The Court: I would like to ask a few questions, Mrs. Harris.

In 1942 your daughter was in school, I understand. What school was she attending?

The Witness: How old was she? I could tell better then.

The Court: Let me see—

Mr. Latham: Sixteen, I will say.

The Witness: She was probably attending either the Flintridge School for Girls, in Pasadena, or she was going to the University High School. I don't remember. She changed— [131.]

The Court: Did she go to college?

The Witness: She is at college now, yes.

The Court: Where is she attending college?

The Witness: The University of Southern California—no, it isn't—now, what is it?

Mr. Latham: University of California at Los Angeles.

The Court: When did she enter, do you remember, when she was a freshman?

The Witness: She was a freshman at Mills College in Oakland. She started at that college.

(Testimony of Anna Harris.)

The Court: When did she start at Mills?

The Witness: I am not good at remembering.

The Court: Immediately after graduating from high school?

The Witness: Yes, whenever that would be.

The Court: Was she sixteen or seventeen when she graduated?

The Witness: Probably seventeen. She must have been about seventeen when she started college.

Th Court: She would have started at Mills in 1943 or 1944, is that right?

The Witness: Probably.

The Court: Now, she is now attending the University of California?

The Witness: That is right. [132]

The Court: What year is she in?

The Witness: I think she is a junior.

The Court: What is she studying?

The Witness: General education.

The Court: General arts course?

The Witness: Well, I don't know exactly. She has changed so much.

The Court: I guess that is all.

Mr. Latham: You may step down.

(Witness excused.)

Mr. Latham: Mr. Harris, will you be sworn and take the stand?

Whereupon,

MORRIS HARRIS,

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Court: State your name, please.

The Witness: Morris Harris.

Direct Examination

By Mr. Latham:

Q. You are Morris Harris, one of the petitioners in this proceeding? A. Yes, sir.

Q. Where do you reside? [133]

A. 10398 Sunset Boulevard.

Q. Los Angeles? A. Los Angeles.

Q. The witness who preceded you is your wife, Mrs. Anna Harris? A. That is right.

Mr. Latham: If your Honor please, to expedite this situation, rather than merely ask the witness the same questions which I asked of the last witness, I would simply like to ask—

By Mr. Latham:

Q. You have heard the testimony of Mrs. Harris, who preceded you on the stand? A. Yes.

Q. Are the statements which she made correct insofar as you know? A. Yes.

Q. Have you anything to add in connection with this situation, to her testimony? A. No.

The Court: Do you want to ask the witness any questions?

Mr. Mather: No, your Honor.

Mr. Latham: That is all.

(Testimony of Morris Harris.)

The Court: I want to ask the witness a few questions. [134]

By the Court:

Q. You went into this business back in the early part of the 1900's, did you? A. 1909.

Q. 1909. How did you acquire your interest in the business; did you purchase it?

A. No, I opened the business; I was the originator of the business.

Q. Do you keep your earnings in the business, build up the capital? A. Yes, I am.

Q. Are you the manager of the business.

A. Yes, I am.

Q. In 1941, about what was the volume of your sales?

A. I couldn't remember offhand; probably around a couple of million dollars; I don't remember exactly but I figure it was—

Q. About how many people did you have; how many employees in 1942?

A. 1942, around 400.

Q. About 400? A. Yes.

Q. Where do you carry on this business; in a plant?

A. In a plant in Los Angeles, and right now we have another place of business in Texas. [135]

Q. In 1942, you had just the plant in Los Angeles?

(Testimony of Morris Harris.)

A. In 1942 we had the place in El Paso, Texas too, a small place.

Q. How many people did you employ in El Paso?

A. Well, in El Paso, off and on, around 300.

Q. In 1942?

A. No, not in 1942. In 1942 probably around 100.

Q. Where is your plant located, in Los Angeles? A. 110 West 11th.

Q. Is that down town? A. Down town.

Q. Do you own the plant?

A. I own the building of the plant, yes.

Q. About how much did you consider your plant was worth, your land and building, in 1942?

A. Well, in 1942 real estate was not very high. Probably around \$300,000, \$350,000, building alone without the equipment.

Q. About \$300,000, \$350,000. What kind of equipment do you have in your plant?

A. All kinds of machinery, sewing machines and everything.

Q. What kind of clothes do you make?

A. Work clothes and sport clothes.

Q. Men's or women's? A. Men's. [136]

Q. How many managers or foremen do you have to have?

A. Well, we have several floorladies upstairs, and then one superintendent.

Q. That was true in 1942?

(Testimony of Morris Harris.)

A. This was true for the last fifteen years.

Q. Do you employ salesmen? A. Yes.

Q. Do you have to do that to sell your goods?

A. Yes.

Q. Where do you sell your goods?

A. Now, all over the United States.

Q. In 1942 did you?

A. In 1942, up to the Rocky Mountains only.

Q. Just on the Pacific Coast and Rocky Mountain region? A. That is right.

Q. About how many salesmen did you employ in 1942?

A. We had, off and on, between 10 and 12.

Q. How did you employ them; on a salary or commission?

A. Commission; all on commission.

Q. About how many customers did you have; did you have a lot of customers or did you just have some main outlets?

A. A long time ago we used to work just in department stores. Right now we sell most of our stuff in chain stores.

Q. But, in 1942 you were selling to chain stores too? A. Yes. [137]

Q. Did you draw a salary in 1942?

A. Yes.

Q. How much was your salary in 1942?

A. I couldn't remember offhand. It seems to me around \$200 a week if I can remember right.

Q. About \$200 a week? A. Yes.

(Testimony of Morris Harris.)

Q. Then what did you do, distribute; did you have a drawing account or distribute profits, at the end of the year to yourself?

A. I had a drawing account against my profits.

Q. Now, after these accounts were set up on the books in 1942, did you have your bookkeeper allocate certain—a certain percent of profits to your son and to your daughter? A. Yes.

Q. What happened to those allocations of profit; did they remain there?

A. They were left in the business.

Q. Children didn't have drawing accounts?

A. They could have drawn if they wanted to, but they didn't.

Q. They didn't draw anything out?

A. No.

Q. Now, when you made that arrangement, your son didn't put any machines or money or anything into the business? [138] A. No, except he—

Q. The answer is, he didn't put in any capital?

A. No capital.

Q. Did he put in any capital, yes or no?

A. He did not.

Q. He wasn't a foreman? A. No.

Q. He was not a salesman?

A. No, he was doing general work.

Q. He was about seventeen?

Mr. Latham: Nineteen.

The Court: But he was doing some work around the plant for three months in his vacation?

(Testimony of Morris Harris.)

The Witness: Yes.

The Court: That is all. I have no other questions of Mr. Harris.

The Witness: He went to a textile school at night.

Mr. Latham: I have just two matters, your Honor.

Mr. Latham:

Q. Mr. Harris, this salary that the Court spoke to you about, was charged against your drawing account? A. Drawing account, yes.

Q. Not in addition to your percentage of profits? A. No.

Q. Albert worked at the company's plant prior to 1942, [139] did he not? A. Yes.

Mr. Latham: I have nothing further.

The Court: Now, on that, he was in school, wasn't he?

The Witness: But whenever he had spare time he used to come over and help us.

Mr. Latham: We will stipulate, of course, that he was in school continuously, except for summer vacations.

The Witness: He was preparing himself to go into the business.

The Court: I guess that is all, Mr. Harris.

(Witness excused.)

Whereupon,

ALBERT P. HARRIS

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: State your name for the record.

The Witness: Albert P. Harris.

Direct Examination

By Mr. Latham:

Q. You are Albert P. Harris?

A. That is right.

Q. You are the son of Mr. Morris Harris and Mrs. Anna [140] Harris who preceded you on the stand?

A. Yes.

Q. How old are you? A. Twenty-four.

Q. And where do you live?

A. 10398 Sunset Boulevard.

The Court: That is your parents' address?

The Witness: Yes.

By Mr. Latham:

Q. You are about to be married?

A. Correct.

Q. What is your occupation?

A. Well, I don't have any title down there. I just do general work, trying to help my father. I sign the checks, I have done some buying made a couple of trips back and forth between the two

(Testimony of Albert P. Harris.)

factories. I wait on customers there—well, I just sort of—

Q. You are connected with the Union Manufacturing Company, are you not? A. Yes, I am.

Q. When did you finish high school?

A. Finished high school in the summer, June 1941.

Q. You were then eighteen years old?

A. Yes.

The Court: What high school did you go to?

The Witness: Los Angeles High.

By Mr. Latham:

Q. In Los Angeles? A. Yes.

Q. Then what did you do?

A. I went back east in September to the University of Virginia, and I went to college there for the next year.

Q. For the year that ended in June of 1942?

A. Yes.

Q. What was the nature of the course that you took there?

A. It was just a general first year, freshman course; nothing specific.

Q. You returned to Los Angeles in the — in June or whenever school was out, in 1942?

A. Yes.

Q. Prior to that time, prior to the summer of 1942, had you worked in the offices or plant of the Union Manufacturing Company?

A. I had been down there off and on helping

(Testimony of Albert P. Harris.)

out. I came down with dad sometimes, with dad on week ends and came down after school at times and helped out.

Q. That was after school during vacation periods?

A. Even earlier than that. I used to come down with my father and work around there, and then after school at times. [142]

Q. Prior to the summer of 1942, had you ever considered with your parents whether or not you would enter that business?

A. Well, it had always been my ambition to go in some day with my father, when I was old enough. That was my intention, when I finished high school, but at that time they wanted me to go to college and I obeyed them and went to college.

Q. You say you wanted to go directly into the business from high school? A. Yes.

Q. Why didn't you?

A. They told me at that time that I would be more help in the business if I have a college education.

Q. When you came back to Los Angeles, we will say, June of 1942, what did you do?

A. Well, at that time I was pretty fed up with college. I had spent a year there like they wanted me to, and I didn't particularly care for it. I didn't want to go—I wanted to go into the business, and I felt like that past year was just wasted. I spent

(Testimony of Albert P. Harris.)

a full four years there and I still would have had to start from scratch, so when I came back then, I told my parents at that time that I didn't care much for it, and that I wanted to go into the business.

They saw that my mind was firmly made up, so at that [143] time there was some talk about my going into the business, but they thought I should have a little more education and it would be best if I had definitely made up my mind at that time to get a little more education in the textile field. So, during that summer I went to U.S.C. and took a course there for the three months I was home, at night, in textiles.

During the day I was down at the factory, helping out, doing various things down there.

Q. You worked throughout the summer at the plant and went to a special textile school at night?

A. Yes, I did.

Q. When the fall of 1942 came, what did you do?

A. The fall of 1942, I went to Raleigh to the textile school, in North Carolina, and I was there until—well, in December, I believe it was, I then enlisted in the Army, because I figured I would rather go in that way than to be drafted, when I saw I would have to go anyway.

I returned home at Christmas and at that time we talked about the partnership, and it was definitely established at that time that the first of

(Testimony of Albert P. Harris.)

next year, that my sister and I would become partners.

I went back there and I was at school until the first part of April.

Q. 1943?

A. Yes, '43, until I was called for active duty.

Q. Called into the Service? A. Yes.

Q. How long were you in the Service?

A. I was in the Service from April, 1943, until January, 1946, when I was discharged. About 33 months.

Q. When you were discharged, what did you do?

A. I immediately went back into the business there. I went in the next week.

Q. Decided you didn't need any more college?

A. Well, I figured what college I could get, I would get at night, and I went to U.S.C. again. I don't know how many more units I took. I also went to U.C.L.A. and took up a bookkeeping course there at night and also went to the business school, Southwestern University Business College and I took some more courses there. I felt they would definitely help me in the business.

Q. Since your discharge from the Army in January of 1946, you devoted all your daylight hours to this business?

A. Yes, I did. All my schooling was at night.

Q. State the nature of your activities since your return?

(Testimony of Albert P. Harris.)

A. You mean when I first came back?

Q. Yes. What in general have you done in the last two years?

A. When I first returned, I wanted to get a thorough [145] knowledge of the business, and I spent most of my time in the factory, for the first couple of months, seeing how our business operated and how the garments were made. Then, as I gradually knew what was going on there, I came down into the office and I waited on customers and helped with the filling of the orders, shipping and so forth like that.

Then, at that time, I also—around that time, I went back east on a buying trip with my uncle. My dad generally went, but I went this time and helped my uncle back there. I had also been to El Paso, our other plant, to handle some matters there.

It was the first of 1947, if I am not mistaken, that my uncle passed away, who was in the business with us, and at that time I fell heir to a lot of work down there. From that time on I was in the office handling most of the sales, customers and buying and handling the checks, signing of the checks and, well—generally, just about everything, so that I could make it as easy as possible on my dad.

Also, I went to El Paso again on some matters over there.

Q. Now, going back to 1942, before you re-

(Testimony of Albert P. Harris.)

turned to North Carolina to school, it had been definitely understood and agreed that as soon as your schooling was completed, or whenever you got out of the Service—

Mr. Mather: Just a moment. Let the witness testify, [146] if you don't mind.

Mr. Latham: I will withdraw that.

By Mr. Latham:

Q. What was your understanding at the time you returned to North Carolina, in the fall of 1942?

A. I definitely understood that, at the end of that year, I would become a partner, along with my sister, Betty?

Q. When was that to be?

A. Well, we had talked about it in June when I came back, and it was my understanding that, at the end of the year, both of us would go in there as partners and when I came home in December of 1942, we definitely, I mean, it was definitely understood then.

Q. Discussed and agreed? A. Yes.

Mr. Latham: That is all.

Cross Examination

By Mr. Mather:

Q. In December when these conversations about a partnership were had, who was present?

A. Mother, daddy, Betty and myself.

Q. Just what was said?

A. Well, we talked about it and my father wanted me to come in for some time. I was anxious

(Testimony of Albert P. Harris.)

to go in then, but they wanted me to go back, so they said they would give me this, [147] but I had to go back though for at least another year. I don't—I mean—exactly what was said at that time, is rather vague now, but it was understood I would go back until at least, I had a knowledge so I could go about the business.

Q. You were still going back to school in December, weren't you? A. Yes, I was.

Q. You did go back to school in North Carolina? A. Yes.

Q. Now, during 1942, did you know anything about the operation of the business?

A. As much as a boy of my age would know about it.

Q. Well, was that any or a lot?

A. As much as anybody would know; probably a little more, because I had an interest in it and I went down there on my own time. I just liked to be down there and see what was going on. It had been my intentions for some time, because my father wanted to sell the business back in '36 or '37, and I told him then that I would like to go in.

Q. You testified that when you came back in 1946, you immediately went into the business and you went down there to learn how garments were manufactured and how the business was operated, didn't you?

A. I wanted a thorough knowledge at that time of everything. I just didn't want to step in down

(Testimony of Albert P. Harris.)

at the office [148] and tell people what to do, when you don't know absolutely everything about it yourself.

Q. Your uncle understood the business and knew how it was operated, did he not?

A. I did have two down there.

Q. But the one you testified with respect to that is no longer with them.

A. He understood a certain phase of the business, he didn't understand it all.

Q. Do you understand all the phases of the business yet?

A. I think as well as you could learn in the couple of years I have been down there.

Q. Do you or don't you understand it all now?

A. Yes.

Q. In helping out, what did your duties consist of, in '42?

A. What do you mean?

Q. Running errands?

A. No. A little more than that. I came down there and filled orders, helped pack merchandise, put away the stock. Generally, during the summer, that is our busy time, and we have an abundance of work down there, and I used to come in during that period and help them fill all the orders and help pack. [149]

Q. About what salary would they pay someone to perform the duties you performed in helping out in 1942?

(Testimony of Albert P. Harris.)

A. I wouldn't know at that time. I know what they pay them now.

Mr. Mather: That is all.

Mr. Latham: We have nothing further.

Mr. Mather: Respondent rests.

Mr. Latham: Petitioner rests.

The Court: How about the bookkeeper? I would like to have the woman that kept the books for the company take the stand. I just have a few questions.

Whereupon,

JUNE GOODENOUGH,

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Court: State your name, please.

The Witness: June Goodenough.

Direct Examination

By the Court:

Q. Now, Miss Goodenough, I want to ask you to give us the facts about the capital set-up of Union Manufacturing Company, prior to January 1, 1942. This business has been in existence since around 1907.

A. 1909 is the date, I believe. [150]

Q. The assets of the business, as I understand it, consisted of, in 1942, two plants, machinery, in-

(Testimony of June Goodenough.)

vested capital, accumulated surplus, and so forth?

A. That is right.

Q. Now, some of the books and accounts of the Union Manufacturing Company have been brought into the Court this morning. Is there anything here in the nature of a balance sheet, as of December 31, 1941, that would show the assets and liabilities of that business?

A. Well, I have not brought any in; not to my knowledge.

The Court: Have you anything of that kind, Mr. Mather?

Mr. Mather: There is a balance sheet, if your Honor please, in the partnership return, one of the partnership returns, and I have balance sheets here for 1942 and 1943.

The Court: Well, it would be helpful to have a balance sheet in evidence, so that we would understand what capital set-up of this business is. Ordinarily, there isn't a place on a partnership return for a balance sheet. It is attached to the partnership return schedule of certain depreciable property, but I think that is all.

Mr. Latham: Here is one which Mr. Mather has for December, 1942 and December, 1943. [151]

By the Court:

Q. Then, I will ask you to look at the balance sheet for December 31, 1942. Now, if you didn't prepare the balance sheet or don't know anything about it, you will have to say so.

(Testimony of June Goodenough.)

A. I did prepare it.

Q. You did prepare that balance sheet. You prepared that from the books of the company?

A. That is right.

Q. That is a true statement of the assets and liabilities? A. Yes, it is.

Q. I show you a balance sheet dated December 31, 1943. Did you prepare that?

A. Yes, I did.

The Court: Now, I would like to have these introduced in evidence by whomever wishes to present them.

Mr. Latham: I will offer these as Petitioners' exhibits, whatever they are, 15 or 16.

Mr. Mather: I thing it is 16 and 17.

The Court: Balance sheet for December 31, 1942, will be received in evidence as Exhibit 16.

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 16.)

[Petitioner's Exhibit No. 16 is set out in full, page 159, of this printed Record.]

The Court: Balance sheet as of December 31, 1943, [152] is received in evidence as Exhibit 17.

(The document above-referred to was received in evidence and marked Petitioners' Exhibit No. 17.)

[Petitioners' Exhibit No. 17 is set out in full, page 160, of this printed Record.]

(Testimony of June Goodenough.)

By the Court:

Q. Now, if you will refer to Exhibit 16, you will find there the capital accounts. Now, what capital account do we have on that balance sheet?

A. For Mr. M. Harris and one for Mrs. A. Harris.

Q. M. Harris and what is the amount of his capital? A. As of the end of the year?

Q. End of 1942. A. \$471,351.04.

Q. Now, Mrs. Anna Harris is shown as having what capital? A. \$465,558.79.

Q. That is the amount after the addition to the previous balance of capital of one-half of 1942 profits, for each, less income taxes and less the amount withdrawn during the year?

Now, we have in evidence capital account of Mr. Morris Harris and Mrs. Anna Harris, Exhibits 12 and 13. Now, will you look at Exhibit 12. You find the balance for his capital account as of December 31, 1941. Would that be \$359,709.94?

A. Yes, because at that time we had two accounts; one [153] for capital, accumulated profit, and we combined them at the end of January, that year.

Q. You did. But, would you help me find that here?

A. That is this figure, \$359—these two added.

Q. You transferred as of January 31, 1942, one-half of accumulated profits to the capital account.

(Testimony of June Goodenough.)

That would be like one-half of surplus, wouldn't it, or accumulated profits?

A. It would mean half, but probably wouldn't be the identical amounts, because the drawings were transferred to that account during the year.

Q. The transfer, \$294,705.94—that gave a total of \$359,705.94. A. Yes.

Q. Was the same transfer made in the case of Mrs. Anna Harris? A. Yes.

Q. Now, we get to Anna Harris' account and you have an entry here, January 31, 1942. This is the credit side, is it not? A. Yes.

Q. On the credit side of the account, transfer some accumulated profits, account journal, 117, \$259,699.14, which made a total of \$334,669.14. That is the balance which is shown on the balance sheet for December 31, 1942 as the total [154] of her capital account.

Now, when these accounts were set up on the books for each one of the children, each was to receive a one-sixteenth interest?

A. That is right.

Q. Now, what did you do to effect that in setting up the capital account for Albert? He received his interest, according to the Petitioners' theory from his mother, so, there would be a reduction, wouldn't there, in her capital account?

A. Yes.

Q. Now, where do you have the reduction in

(Testimony of June Goodenough.)

her capital account? His account is opened, isn't it?

A. As a matter of fact, the two names were switched here. That would be Albert and the other Betty, but there is the same amount involved.

Q. Now, wait a minute, according to the books, it was Morris Harris' capital account which was charged with some amount for a new capital account for Albert, is that right?

A. That is right.

Q. And his account was charged on September 16, 1943, with \$34,083.70; is that right?

A. That is right.

Q. Then, was the capital account for Albert opened with that amount? [155]

A. That is right.

Q. Where do we find that?

A. The top figure.

Q. We find that account opened then, as of January 1, 1943, although the transfer was made on September 16, 1943? A. That is right.

Q. Then, the capital account of Anna Harris, Mrs. Anna Harris, was charged on September 16, 1943, with \$34,083.70 and as of January 1, 1943, a capital account was opened in the name of Betty by an entry of \$34,083.70, is that right?

A. That is right.

Q. Now, then, looking at the account for Albert and Betty, what do we have here? As of December 31, 1943, we have a credit of \$21,870.95 in his

(Testimony of June Goodenough.)

account, and a credit in Betty's account of the same amount, and that is supposed to be what?

A. One-sixteenth share of the profits for the year.

Q. 1943? A. Yes.

Q. Now, the debit in each account for 1943 is \$9,879.79. What was that for?

A. That is to pay the estimated income tax for 1943.

Q. Federal and state or federal?

A. Federal.

Q. Just federal? A. Federal. [156]

Q. Now, the debit entries were to represent withdrawals, wouldn't they?

A. Yes, your Honor.

Q. The credit entries represent increases in the account? A. Yes.

Q. So, with that explanation we can understand these exhibits, is that right? A. Yes.

The Court: Do you want to ask the witness any questions?

Mr. Mather: There is one question I would like to ask.

Cross Examination

By Mr. Mather:

Q. You spoke of two businesses. They didn't acquire the El Paso business until 1943, did they?

A. 1940. It is the same business, however.

Q. Was it a new building they bought down in El Paso in 1943?

(Testimony of June Goodenough.)

A. I believe it was. The building was acquired at that time, at the present location.

Mr. Mather: I have nothing further.

The Court: That concludes the hearing in this proceeding, and the dates will be read now by the clerk for [157] the briefs, allowing 15 days extra time for reply briefs.

The Clerk: March 16 for the original briefs and reply briefs on April 16.

(Whereupon, at 4:30 o'clock p.m., Thursday, January 29, 1948, the hearing in the above-entitled matter was closed.)

[Endorsed]: T.C.U.S. Filed Feb. 20, 1948. [158]

PETITIONERS' EXHIBIT No. 1

Form 540

State of California—Income Tax Division

INDIVIDUAL INCOME TAX RETURN—RESIDENT

For Gross Incomes of More Than \$5,000 From Salaries, Wages, Dividends, Interest, Annuities, and for Incomes From Other Sources Regardless of Amounts (See Instruction B).

For Calendar Year 1942

of fiscal year begun....., 1942, and ended....., 1943

MORRIS HARRIS

10398 Sunset Boulevard, Los Angeles, California

1. Are you a resident of the State of California? Yes.
2. Were you married and living with husband or wife during taxable year? Yes.
3. Are all items of income or deductions of both husband and wife included in this return? No.
4. State (a) Name of husband or wife if a separate return was made: Anna Harris.

* * * *

6. How many dependent persons (other than husband or wife) received their chief support from you during your taxable year: (a) Under eighteen years of age: Three.

* * * *

8. Check whether this return was prepared on the cash [x] or accrual [] basis.
9. State your principal occupation or profession: Partner—Union Mfg. Co.
10. Did you file a state return for any prior year? Yes. If so, what was the latest year? 1941.
11. Did you file a return with the Federal Government for 1942, or fiscal year stated herein? Answer "yes" or "no": Yes.
12. If the answer to No. 11 is "yes," state amount of net income (or loss) reported on the Federal return. Net income (or loss): \$228,931.78.
13. Has the Federal Government assessed or proposed to assess any additional income tax for 1940: No. 1941: No.

INCOME

* * * *

2. Dividends	\$ 504.37
3. Interest on (a) bank deposits, notes, etc., \$.....;	
(b) corporation bonds \$.....,	17.52
* * * *	
5. Rents and royalties (from Schedule B).....	17,495.06
* * * *	
8. Income (or loss) from partnerships, syndicates, pools, etc. (furnish names and addresses) Union Manufacturing Co., 110 West 11th St. L. A.....	227,235.34
9. Income from fiduciaries (furnish names and addresses) Union Ranch, 110 West 11th St., L.A.	729.67
* * * *	
11. Total Income in Items 1 to 10.....	\$245,981.96

DEDUCTIONS

12. Contributions (explain in Schedule E)	
See schedule	\$ 1,581.37
* * * *	
14. Taxes (explain in Schedule E) See schedule.....	2,860.23
* * * *	
18. Total Deductions in Items 12 to 17.....	\$ 4,441.60
19. Net Income (Item 11 minus Item 18).....	\$241,540.36

COMPUTATION OF TAX (See Instruction 24)

20. Net Income (Item 19 above).....	\$241,540.36	
21. Less: Personal exemption (See Instructions 21-22)	\$2,500.00	
22. Credit for dependents.....	1,200.00	3,700.00
		<hr/>
23. Balance subject to Tax.....	\$237,840.36	
24. Tax (See Instruction 24).....	\$ 26,747.65	
* * * *		<hr/>
26. Balance of Tax.....	\$ 26,747.65	

AFFIDAVIT (See Instruction F)

I swear (or affirm) that this return (including its accompanying schedules and statements, if any) has been examined by me, and to the best of my knowledge and belief is a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to The Personal Income Tax Act.

This declaration made under penalty of perjury
(If return is made by agent, the reason therefore must be
stated on this line.)

.....
(Signature) (See Instruction F)

.....
(Signature)

(If this is a joint return (not made by agent), it must be signed by both husband and wife, but it need be sworn to before a proper officer only by the spouse preparing the return. If neither or both prepare the return, it must be sworn to by both spouses.)

Subscribed and sworn to by.....before
me this.....day of March, 1943.

.....
(Signature and title of officer administering oath.)

SCHEDULE A—Interest on State, Municipal, and Other
Bonds or Obligations (See Instruction 4)

1. Bonds or Obligations	2. Amount Owned	3. Interest Received or Accrued
* * * *		
(b) Obligations of the United States, or of the District of Columbia.....	\$38,000.00	\$97.50
* * * *		

MORRIS HARRIS—1942 CONTRIBUTIONS

Line 12

One-half contributions \$1209.86

Union Manufacturing Company—a partnership. University Religion Conference \$10.00; Friday Morning Club Fund \$2.50; Los Angeles Science League \$2.20; U. S. O. \$43.00; Council Thrift Shop \$5.75; Open House Fund \$20.00; Temple Sisterhood \$3.50; Westwood Auxiliary Defense \$10.00; Haddassah Fund \$9.90; Los Angeles Philamarnic Fund \$5.00; Hollywood Guild \$10.00; Home for Aged \$3.00; Women's Emergency Corps, \$10.00; Russian Relief \$16.50; Wilshire Boulevard Temple \$100.00; Vista Del Mar Fund \$8.50; Council of Jewish Women \$28.91; Julia Ann Nursery \$5.00; Red Cross \$15.00; Helping Hand \$59.25; Community Center \$3.50—Total \$1581.37

Line 14—Federal

City & County taxes \$2651.37; Auto License taxes \$48.80; Auto Stamp taxes \$27.21; Amusement taxes \$81.12; Phone taxes \$30.53; U. S. Luxury taxes \$21.20; Gasoline taxes, \$45.75; Sales taxes \$155.49; Calif. Income taxes \$12,407.34—Total \$15,468.81.

Line 14—State of Calif.

City & County taxes \$2651.37; Auto License taxes \$48.80; Auto stamp taxes \$27.21; Amusement taxes \$81.12; Phone taxes \$30.53; U. S. Luxury taxes \$21.20—Total \$2860.23.

Morris Harris, Los Angeles, Calif.—1942

	Rents	Deprec.	Rep.	Other Exp.	Profit & Loss
Brick	\$29,880.00	\$4,383.14		\$7,828.61	\$17,668.25
Stucco	2,100.00	1,100.00	\$44.91	1,128.28	173.19*
			Gain.....		\$17,495.06

* Loss

Line 1—Insurance \$772.53; Interest \$3937.50; Taxes \$3118.58—Total \$7828.61.

Line 2—Gardner \$246.59, fertilizer \$24.72, cleaning \$179.00, insurance \$25.00, taxes \$594.93, association dues \$12.00, lighting \$46.04—Total \$1128.28.

Schedule of Depreciation

	Acq.	Cost	Deprec. Allowed	Rem. Cost	Life	1942
Line 1—						
brick	1923	\$219,387.19	\$74,529.34	\$144,857.85	2%	\$4,383.14
Line 2—						
stucco		22,000.00	1,600.00	20,400.00	5%	1,100.00

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948.

 PETITIONERS' EXHIBIT No. 2

Form 540

State of California—Income Tax Division

INDIVIDUAL INCOME TAX RETURN—RESIDENT

For Gross Incomes of More Than \$5,000 From Salaries, Wages, Dividends, Interest, Annuities, and for Incomes From Other Sources Regardless of Amounts (See Instruction B)

For Calendar Year 1942

or fiscal year begun....., 1942, and ended....., 1943

ANNA HARRIS

10398 Sunset Blvd., Los Angeles, Calif.

1. Are you a resident of the State of California? Yes.
2. Were you married and living with husband or wife during your taxable year? Yes.
3. Are all items of income or deductions of both husband and wife included in this return? No.
4. State (a) Name of husband or wife if a separate return was made: Morris Harris.

* * * *

8. Check whether this return was prepared on the cash [x] or accrual [] basis.
9. State your principal occupation or profession: Partner Union Mfg. Co.
10. Did you file a state return for any prior year? Yes. If so, what was the latest year? 1941.

11. Did you file a return with the Federal Government for 1942, or fiscal year stated herein? Answer "Yes" or "No": Yes.
12. If the answer to No. 11 is "Yes," state amount of net income (or loss) reported on the Federal return. Net income (or loss): \$215,785.09.
13. Has the Federal Government assessed or proposed to assess any additional income tax for 1940: No. 1941: No.

INCOME

* * * *	
2. Dividends	\$ 1,664.38
3. Interest on (a) bank deposits, notes, etc., \$.....;	
(b) corporation bonds, \$.....,	125.71
* * * *	
5. Rents and royalties (from Schedule B).....	*628.56
* * * *	
9. Income from fiduciaries (furnish names and addresses) Union Manufacturing Co., 110 West 11th St., L. A.....	227,235.34
* * * *	
11. Total Income in Items 1 to 10.....	\$228,396.87
* Loss.	

DEDUCTIONS

12. Contributions (explain in Schedule E).....	\$ 1,209.86
* * * *	
18. Total Deductions in Items 12 to 17.....	\$ 1,209.86
19. Net Income (Item 11 minus Item 18).....	\$227,187.01

COMPUTATION OF TAX (See Instruction 24)

20. Net Income (Item 19 above).....	\$227,187.01
21. Less: Personal exemption (See Instructions 21-22)—Taken by husband	
* * * *	
23. Balance subject to Tax.....	\$227,187.01
24. Tax (See Instruction 24)	\$ 25,256.18
* * * *	
26. Balance of Tax.....	\$ 25,256.18

AFFIDAVIT (See Instruction F)

I swear (or affirm) that this return (including its accompanying schedules and statements, if any) has been examined by me, and to the best of my knowledge and belief is a true, correct, and

complete return, made in good faith, for the taxable year stated, pursuant to The Personal Income Tax Act.

This declaration made under penalty of perjury
(If return is made by agent, the reason therefor must be
stated on this line)

(Signature) (See Instruction F)

(Signature)

(If this is a joint return (not made by agent), it must be signed by both husband and wife, but it need be sworn to before a proper officer only by the spouse preparing the return. If neither or both prepare the return, it must be sworn to by both spouses.)

Subscribed and sworn to by.....before me
this.....day of194....

(Signature and title of officer administering oath.)

SCHEDULE A—Interest on State, Municipal, and other Bonds
or Obligations (See Instruction 4)

1. Bonds or Obligations	2. Amount Owned	3. Interest Received or Accrued
* * * *		
(b) Obligations of the United States, or of the District of Columbia.....	\$18,000.00	\$97.50
* * * *		

SCHEDULE B—Income from Rents and Royalties
(See Instruction 5)

1. Kind of Property	2. (Explain in Amount Sched. F)	3. Deprec. Amount	4. Repairs (Explain below)	5. Other Ex- penses (Item- ize below)
No rent received	none	\$300.00	\$87.93	\$240.63

Explanation of deductions claimed in Columns 4 and 5:
Gardner \$75.00; insurance \$12.50; taxes 150.58; lighting \$2.55—
Total \$240.63.

[Endorsed]: T.C.U.S. Admitted in evidence Jan.
29, 1948.

PETITIONERS' EXHIBIT No. 3

This Agreement, made in duplicate and entered into this 2nd day of January, 1924, by and between Morris Harris and Anna Harris, husband and wife:

Whereas, the above named parties are desirous of associating themselves together for the purpose of carrying on the business of manufacturing work clothing, and,

Whereas, the said Morris Harris is now the sole owner of the following described property and the business known as the Union Manufacturing Company:

Inventory of stock on hand.....	\$75,563.49
Accounts receivable	42,220.95
Insurance (prepaid)	246.28
Fixtures	358.40
Machinery	2,622.50
Stationery	188.79

Now, Therefore, the said Morris Harris for and in consideration of the sum of ten dollars and other good and valuable considerations, receipt whereof is hereby acknowledged does hereby grant, bargain, sell and convey unto the said Anna Harris a one-half interest in the above mentioned property.

It is mutually agreed by and between the respective parties hereto that all of the hereinbefore mentioned property shall immediately become partnership property to be used in the business known as the Union Manufacturing Company.

It is mutually agreed by and between the respective parties hereto that they shall and will, at all

times during the continuance of this agreement, bear, pay and discharge equally between them, all expense that may be required for the support [165] and management of said business; that all gains, profits and increase that shall come, grow or arise, from or by means of said business shall be divided between them share and share alike, and all loss that shall happen their joint business shall be borne and paid equally between them; that there shall be kept at all times during the continuance of this agreement just and true books of account.

This agreement shall remain in full force and effect for the term of ten years from the date hereof unless sooner abrogated and cancelled by mutual consent of the parties hereto.

In Witness Whereof, the parties hereto have set their hands.

MORRIS HARRIS

ANNA HARRIS

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948.

PETITIONERS' EXHIBIT No. 5

Form 1065

United States

PARTNERSHIP RETURN OF INCOME 1944

(To be Filed Also by Syndicates, Pools, Joint Ventures ,Etc.)

For Calendar Year 1944

or fiscal year beginning....., 1944, and ending....., 1945

[Stamped]: Serial No. 8719718. Received Mar. 15, 1945. Coll.

Int. Rev., Los Angeles, Cal. No. 4.

UNION MANUFACTURING COMPANY
110 West 11th Street, Los Angeles, California

Business or Profession: Mfgs. Men's work clothing

GROSS INCOME

1. Gross receipts from business or profession.....\$ 2,613,164.81

2. Less cost of goods sold:

(a) Inventory at beginning

of year\$ 586,878.36

(b) Merchandise bought

for sale 1,377,256.16

(c) Cost of labor, supplies, etc. 468,002.79

(d) Total of lines (a),

(b), and (c) 2,432,137.31

(e) Less inventory at end

of year 363,772.63 2,068,364.68

3. Gross profit (or loss) from business or pro-

fession (item 1 less item 2).....\$ 544,800.13

* * * *

8. Rents 1,251.94

* * * *

12. Other income (state nature of income) :

Discounts on Purchases 7,225.54

13. Total income in items 3 to 12.....\$ 553,277.61

DEDUCTIONS

14. Salaries and wages (do not include compensa-

tion for partners).....\$ 182,540.52

15. Rent 26,700.00

* * * *

17. Interest on indebtedness (explain in Sched. F) 5,479.32

18. Taxes (explain in Schedule C)..... 30,664.15

* * * *

21. Depreciation (explain in Schedule E)..... 8,056.30

* * * *

24. Other deductions authorized by law
(explain in Schedule F)..... 66,383.55

25. Total deductions in items 14 to 24.....\$ 319,823.84

26. Ordinary net income (item 13 less item 25).....\$ 233,453.77

* * * *

[Stamped on face of page 1]: Revenue Agent in Charge, Los
Angeles Division. Received Sep 18, 1945. Field.

* * * *

SCHEDULE C.—TAXES. (See Instruction 18)

Nature	Amount
City and county taxes.....	\$ 9,079.23
License	322.00
El Paso, Texas.....	4,295.64
Social Security	16,967.28
Total (enter as item 18, page 1).....	\$ 30,664.15

* * * *

SCHEDULE E.—DEPRECIATION. (See Instruction 21)

See Schedule	9. Depreciation al- lowable this year
Total (enter as item 21, page 1).....	\$8,056.30

SCHEDULE F.—EXPLANATION OF DEDUCTIONS
CLAIMED IN ITEMS 17 AND 24

1. Item No.	2. Explanation	3. Amount
	See Schedule	
		\$66,383.55

* * * *

SCHEDULE H.—CONTRIBUTIONS OR GIFTS PAID
(See Instruction for Schedule I)

Name and address of organization	Amount
See Schedule	
Total (enter in column 9, Schedule I).....	\$7,515.37

SCHEDULE I.—PARTNERS' SHARES OF INCOME AND CREDITS (See Instruction for Schedule I)

1. Name and address of each partner	2. Ordinary net income less interest on Government obligations, etc.
(a) Morris Harris, 10398 Sunset Blvd., Los Angeles	\$102,136.03
(b) Anna Harris, 10398 Sunset Blvd., Los Angeles	102,136.02
(c) Albert Harris, 10398 Sunset Blvd., Los Angeles	14,590.86
(d) Betty Harris, 10398 Sunset Blvd., Los Angeles	14,590.86
Totals	\$233,453.77

Continuation of Schedule I

9. Charitable Contributions (From Schedule H)
\$3,287.98
3,287.97
469.71
469.71
Total
\$7,515.37

QUESTIONS

1. Date of organization: 1909.
2. Nature of organization (partnership, syndicate, pool, joint venture, etc.): Partnership.
3. Was a return of income filed for preceding year? Yes. If so, to which collector's office was it sent? Los Angeles.
4. Check whether this return was prepared on cash [] or accrued [x] basis.
5. State whether inventories at the beginning and end of the taxable year were valued at (a) cost, or (b) cost or market whichever is lower: Cost or market whichever is lower.
6. Did the organization at any time during the taxable year own directly or indirectly any stock of a foreign corporation or of a personal holding company, as defined in section 501 of the Internal Revenue Code): (Answer "Yes" or "No"): No.
7. Was return of information on Forms 1096 and 1099, Form W-2 or Form W-2a, filed for the calendar year 1944: Yes. (See Instruction H.)

AFFIDAVIT (See Instruction D)

I swear (or affirm) that this return (including any accompanying schedules and statements) has been examined by me, and to the best of my knowledge and belief is a true, correct, and complete return.

/s/ ANNA HARRIS

Date 3/9/45

(Partner or member)

110 West 11th Street, Los Angeles, Calif.

/s/ D. WEBSTER EGAN

Date 3/9/45

(Signature of person (other than partner or member) preparing return)

Subscribed and sworn to before me this 12th day of March, 1945.

/s/ FRANK LOBER,

(Signature of officer administering oath)

Union Manufacturing Company—1944

SCHEDULE OF DEPRECIATION

	Acq.	Cost	Dep. Allowed	Rem. Cost	Life	Dep. 1944
Auto	1940	1965.45	1597.05	368.40	25%	368.40
Furniture	1940	319.83	124.19	195.64	10%	31.98
“	1941	168.95	33.80	135.15	10%	16.90
“	1942	332.15	66.42	265.73	10%	33.21
“	1943	145.50	2.03	143.47	10%	14.00
Machinery	1935	7713.26	6987.20	726.96	10%	726.06
“	1936	12799.72	10429.04	2370.68	10%	1185.44
“	1937	1803.78	1050.85	752.93	10%	180.38
“	1938	3434.69	1916.87	1517.82	10%	343.47
“	1939	4736.66	2174.76	2561.90	10%	473.36
“	1940	7164.57	992.83	6171.74	10%	716.45
“	1941	12518.26	4640.61	7877.65	10%	1251.83
“	1942	13921.70	2754.37	11167.33	10%	1392.17
“	1943	1797.47	112.00	1685.47	10%	179.75
“	1944	7766.51	0.00	7766.51	10%	395.40
Buildings	1944	32500.00	0.00	32500.00	2%	650.00
“	1944	6500.00	0.00	6500.00	5%	97.50

 8056.30

Other deductions: Auto Expense 630.75; Discounts 8177.77;
 Dues and Assessments 1644.29; General Expense 38088.16;
 Insurance 6267.10; Telephones and Telegrams 1298.21;
 Travel Expense 4974.20; Utilities 5303.07. Total: 66,383.55.

Contributions: Palestine Society 10.00; Central Jewish Committee \$5.00; West Gate Lodge Fund 2.00; War Chest 1000.00; Red Cross 2000.00; Naval Aid 121.37; Orthopaedic Foundation 500.00; Boy Scouts 12.00; Home for Aged 20.00; Wilshire Blvd. Temple 1000.00; Evely Smith Fund 25.00; Boys Camp 10.00; American Council for Judaism 10.00; El Nido Camp 300.00; Jewish Welfare 2500.00; Total 7515.37.

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948.

PETITIONERS' EXHIBIT No. 6

Form 1065 United States
 PARTNERSHIP RETURN OF INCOME 1943
 (To be Filed Also by Syndicates, Pools, Joint Ventures, Etc.)

For Calendar Year 1943
 or fiscal year beginning....., 1943, and ending....., 1944

UNION MANUFACTURING COMPANY,
 110 West 11th Street, Los Angeles, 15, California

Serial No. 988045 [Stamp] Mar. 15, 1944

GROSS INCOME

- | | | | |
|---------|---|-----------------|--------------|
| 1. | Gross receipts from business or profession..... | \$ 2,858,253.17 | |
| 2. | Less cost of goods sold: | | |
| | (a) Inventory at beginning | | |
| | of year | \$ 538,992.70 | |
| | (b) Merchandise bought | | |
| | for sale | 1,788,851.00 | |
| | (c) Cost of labor, supplies, etc. | 456,875.99 | |
| | (d) Total of lines (a), | | |
| | | 2,784,719.69 | |
| | (e) Less inventory at end | | |
| | of year | 586,878.36 | 2,197,841.33 |
| 3. | Gross profit (or loss) from business or
profession (item 1 minus item 2)..... | | 660,411.84 |
| * * * * | | | |
| 11. | Net gain (or loss) from sale or
exchange of property other
than capital assets (from
Schedule B) | \$ 352.56 | |

144 *Anna Harris and Morris Harris vs.*

* * * *

13. Other income (state nature of
income) Discount on purchases 9,343.95

14. Total income in items 3 to 13 (enter non-
taxable incomes in Schedules A and G).....\$ 670,108.35

DEDUCTIONS

15. Salaries and wages (do not include
compensation for partners).....\$176,159.38

16. Rent 26,700.00

* * * *

18. Interest on indebtedness (explain
in Schedule F)..... 2,786.31

19. Taxes (explain in Schedule C)..... 32,807.89

* * * *

22. (a) Depreciation (explain in
Schedule E) 7,401.39

* * * *

24. Other deductions authorized by
law (explain in Schedule F)..... 43,340.80

25. Total deductions in items 15 to 24.....\$289,195.77

26. Ordinary net income (item 14 minus item 25).....\$380,912.58

* * * *

SCHEDULE B.—GAINS AND LOSSES FROM SALES OR
EXCHANGES OF PROPERTY OTHER THAN CAPITAL
ASSETS (See Instruction 11)

1. Kind of property	2. Date acquired	3. Gross sales price (contract price)	4. Cost or other basis
Sewing machine	1935	\$100.00	\$ 350.00
Sewing machine	1936	704.00	1271.00

Schedule B—(Continued)

6. Depreciation allowed (or allowable) since ac- quisition or March 1, 1913 (furnish details)	7. Gain or loss (col. 3 plus col. 6 minus the sum of cols 4 and 5)
\$280.00	30.00
889.56	322.56

Total net gain (or loss) (enter as item 11, p. 1) \$352.56

SCHEDULE C.—TAXES (See Instruction 19)

Nature	Amount
City & County	\$11,663.64
	21,144.25
	<hr/>
Total (enter as item 19, page 1).....	\$32,807.89

* * * *

SCHEDULE J.—PARTNERS' SHARES OF INCOME AND CREDITS (See Instruction 29)

1. Name and addresses of each partner	2. Ordinary net income less interest on Government ob- ligations, etc., subject to surtax only
(a) Morris Harris, 10398 Sunset Blvd., L. A.	\$166,649.25
(b) Anna Harris, 10398 Sunset Blvd., L. A.	166,649.25
(c) Albert Harris, 10398 Sunset Blvd., L. A.	23,807.04
(d) Betty Harris, 10398 Sunset Blvd., L. A.	23,807.04
	<hr/>
Total.....	\$380,912.58

Schedule J—(Continued)

5. Use letter corre- sponding to above to identify partner	10. Charitable contributions (from Schedule I)
(a)	\$ 5,590.15
(b)	5,590.15
(c)	798.60
(d)	798.60
	<hr/>
Total.....	\$12,777.50

QUESTIONS

1. Date of organization: 1909.
2. Nature of organization (partnership, syndicate, pool, joint venture, etc.): Partnership.
3. Was a return filed for preceding year: Yes. If so, to which collector's office was it sent): Los Angeles.
4. Check whether this return was prepared on the cash [] or accrual [x] basis.
5. State whether inventories at the beginning and end of the taxable year were valued at (a) cost, or (b) cost or market, whichever is lower: Cost or market whichever is lower.

6. Did the organization at any time during its taxable year have in its employ more than eight individuals? (Answer "Yes" or "No"): Yes. * * *
7. Did the organization at any time during the taxable year own directly or indirectly, any stock of a foreign corporation or a personal holding company as defined in section 501 of the Internal Revenue Code? (Answer "Yes" or "No"): No.
8. Was return of information on Forms 1096 and 1099, or Forms V-2 and W-2, filed for the calendar year 1943? (See Instruction H): Yes.

AFFIDAVIT (See Instruction D)

I/we swear (or affirm) that this return (including any accompanying schedules and statements) has been examined by me/us, and to the best of my/our knowledge and belief is a true, correct, and complete return, made in good faith, for the accounting period stated, pursuant to the Internal Revenue Code and the regulations issued under authority thereof.

/s/ ANNA HARRIS Date 3/10/44
(Partner or member)
10398 Sunset Blvd., Los Angeles, Calif.

/s/ D. WEBSTER EGAN Date 3/10/44
(Signature of person (other than partner or
member) preparing return)
403 W. 8th St., Los Angeles, Calif.

Subscribed and sworn to before me this 15th day of March,
1944.

/s/ HARRY DAVID KROLL,
Notary Public in and for the City and County of Los Angeles,
State of California.

Union Manufacturing Company—1943

	Acquired	Cost	Depreciation	Remaining		Estimated	
				Cost	Life	Remaining Life	Deprec. 1943
Automobile	1940	1965.45	1105.65	859.80	4 yr.	1 yr.	491.40
Furniture	1943	145.50	0.00	145.50	10 yr.	10 yr.	2.03
"	1942	332.15	33.21	298.94	10 yr.	9 yr.	33.21
"	1941	168.95	16.90	152.05	10 yr.	9 yr.	16.90
"	1940	319.83	92.21	227.62	10 yr.	7 yr.	31.98
"	Prior	191.38	177.10	14.28	10 yr.	1 yr.	14.28
Machinery—L.A.	1933	1258.73	1191.02	67.71	10 yr.		62.84
"	1934	2319.37	1971.49	347.88	10 yr.	1 yr.	231.94
"	1935	7499.57	5682.20	1817.37	10 yr.	2 yr.	749.95
"	1936	13142.53	8542.63	4218.46	10 yr.	3 yr.	1314.25
"	1937	1159.00	637.45	521.55	10 yr.	4 yr.	115.90
"	1938	3277.40	1474.83	1802.57	10 yr.	5 yr.	327.74
"	1939	1691.48	3141.31	483.28	10 yr.	6 yr.	483.28
"	1940	2549.27	737.90	1811.37	10 yr.	7 yr.	254.93
"	1941	1082.50	225.25	857.25	10 yr.	8 yr.	108.25
"	1942	1097.35	97.23	1000.12	10 yr.	9 yr.	109.74
"	1943	2070.31	0.00	2070.31	10 yr.	10 yr.	103.50
Machinery—E.P.	1935	616.81	493.37	123.44	10 yr.	2 yr.	61.68
"	1936	715.25	500.64	214.61	10 yr.	3 yr.	71.52
"	1937	425.00	255.00	170.00	10 yr.	4 yr.	42.50
"	1938	190.55	95.25	95.30	10 yr.	5 yr.	19.05
"	1941	14723.17	2834.70	11888.38	10 yr.	8 yr.	1472.32
"	1942	12737.03	1273.70	11463.33	10 yr.	9 yr.	1273.70
"	1943	105.05	0.00	105.05	10 yr.	10 yr.	8.50

CONTRIBUTIONS

American Red Cross \$1610.00, S. C. Symphony Assn. \$50.00, United Nations W.R. \$100.00, Los Angeles Community Chest, \$1200.00, L. A. Hadassah \$5.00, Central Jewish Com. \$5.00, U. S. O. \$1500.00, African M. E. Church \$5.00, Home for Aged-Jewish \$100.00, Children's Hospital \$500.00, T. B. Christmas seals \$2.00, Filipino Bolo Knife \$5.00, Tuskegee Institute \$1.00, E. P. Community Chest \$100.00, West Gate Lodge F & M \$10.00, K.R.O.D.-El Paso \$10.00, Police Pension Fund \$33.00, V.D.M. Orphans Home \$2000.00, Boy Scouts-El Paso \$12.00, Passover Relief Bur. \$5.00, L. A. Orthopaedic Fd. \$500., Shrine Fund-El Paso \$7.50, N. Strauss Palestine \$10.00, Jewish Blind \$2.00, United Jewish Welfare \$5000.00, Veterans Army News \$5.00—
Total \$12,777.50.

Auto expense	\$ 577.71
Discount on sales	12,642.07
Dues and assessments	1,477.77
General expense	15,429.12
Gas	792.45
Insurance	4,661.59
Power and Light	4,226.23
Telephones and Telegrams.....	1,229.49
Travel expense	2,091.42
Water	212.95

\$43,340.80

All salary increases have been made in accordance with the established custom of firm and in compliance with War Labor Board regulations.

Field.

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948. [179]

PETITIONERS' EXHIBIT No. 7

Form 709

United States

GIFT TAX RETURN

Calendar Year 19.....

Donor: Anna Harris Address: 10398 Sunset Blvd., L. A.
Citizenship: American Residence: Same

Have you (the donor) during the calendar year indicated above, without an adequate and full consideration in money or money's worth, made any transfer exceeding \$4,000 in value (or regardless of value if in trust or a future interest) as follows?

(Answer "Yes" or "No")

1. By the creation of a trust (No) or the making of additions to a trust previously created (No), in either case for the benefit of a person or persons other than yourself, and with respect to which you retain no power to revest the beneficial title to the property in yourself or to change the beneficiaries or their proportionate benefits; or by relinquishing every such power that was retained in a previously created trust (No).
2. By permitting a beneficiary, other than yourself, to receive the income from a trust created by you and with respect to which you retained the power to revest the beneficial title to the property in yourself or to change the beneficiaries or their proportionate benefits (No).
3. By the purchase of a life insurance policy (No) or the payment of a premium on a previously issued policy (No) the proceeds of which are in either case payable to a beneficiary other than your estate, and with respect to which you retained no power to revest the economic benefits in yourself or your estate or to change the beneficiaries or their proportionate benefits; or by relinquishing every such power that was retained in a previously issued policy (No).
4. By permitting another to withdraw funds from a joint bank account which was deposited by you (No).
5. By conveying title to another and yourself as joint tenants or to your wife or husband and yourself as tenants by the entirety (No).
6. By any other method, direct or indirect (Yes).

If the answer is "Yes" to any of the foregoing, such a transfer should be fully disclosed under Schedule A.

COMPUTATION OF AMOUNT OF NET GIFTS FOR YEAR

1. Total included amount of gifts for year
(item c, schedule A)\$30,000.00
2. Total deductions for charitable, public,
and similar gifts for year (item c,
schedule B) None
3. Specific exemption claimed (see sec-
tion 10 of instructions).....\$30,000.00
4. Total deductions (item 2 plus item 3).....\$30,000.00
5. Amount of net gifts for year (item 1 minus item 4) None

COMPUTATION OF TAX (see section 14 of instructions)

* * * *

8. Total tax payable for year (item 6 plus item 7)..... None

AFFIDAVIT OF PERSON PREPARING RETURN

I swear (or affirm) that I prepared this return for the person named herein and that this return, including the accompanying schedules and statements, if any, is a true, correct, and complete statement of all the information respecting the donor's gift tax liability of which I have any knowledge.

.....
(Signature of person preparing return)

.....
(Address of person preparing return)

Sworn to and subscribed before me this 27th day of Sept., 1943.

.....
(Signature and title of officer administering oath)

SCHEDULE A—Total Gifts During Year (see sections 5, 6, 7, 9, 11, and 15 of instructions)

Description of gift, and Donee's name and address	Date of gift	Value at date of gift
An undivided 1/16 Interest in and to the property and assets of Union Mfg. Co., L. A., Cal., a partnership. Albert P. Harris, 10398 Sunset Blvd., L.A.	1/2/43	\$33,000.00

- | | |
|--|--------------|
| (a) Total | \$ 33,000.00 |
| (b) Less total exclusions not exceeding \$4,000 for each
donee (except gifts in trust or of future interests) | 3,000.00 |
| (c) Total included amount of gifts for year..... | \$ 30,000.00 |

SCHEDULE B.—Deductions for Charitable, Public, and Similar Gifts During Year (see sections 8, 9, and 12 of instructions)
None

SCHEDULE C.—Returns, Amounts of Specific Exemption, and Net Gifts for Preceding Year (subsequent to June 6, 1932)
None

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948.

PETITIONERS' EXHIBIT No. 8

Treasury Department, Internal Revenue Service

Form 710

GIFT TAX

DONEE'S OR TRUSTEE'S INFORMATION
RETURN OF GIFTS

Calendar Year 19.....

Donor's name: ANNA HARRIS.

Donor's address: 10398 Sunset Blvd., L. A.

Donee's name: ALBERT P. HARRIS.

Donee's address: 10398 Sunset Blvd., L. A.

Description of property received	Date of gift	Approx. value at date of gift
An undivided one-sixteenth interest in and to the property and assets of the Union Mfg. Co., a partnership.	1/2/43	\$33,000.00

Pursuant to the Gift Tax Regulations of the Treasury Department, I hereby give notice of the herein-described property received from the above-named donor, and certify that I have carefully read the instructions on the reverse side of this form and that all the information given herein is correct, to the best of my knowledge and belief.

(Signature).....

(Designation).....

(Address if donee's executor or administrator)

Date....., 19.....

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948. [182]

PETITIONERS' EXHIBIT No. 9

[This exhibit is identical with Exhibit No. 7 set out at page 149 with the exception of donor's name which is Morris Harris for Exhibit No. 9.]

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948. [183]

PETITIONERS' EXHIBIT No. 10

[This exhibit is identical with Exhibit No. 8 set out at page 151 with the exception of donor's name which is Morriss Harris for Exhibit No. 10.]

[Endorsed]: T.C.U.S. Admitted in evidence Jan. 29, 1948. [185]

PETITIONERS' EXHIBIT No. 11

Mailed 10/2/45

Treasury Department

Internal Revenue Service

Twelfth Floor, 417 So. Hill St.

Los Angeles, Calif.

Office of Internal Revenue Agent in Charge, Los Angeles Division

September 25, 1945

Mr. D. Webster Egan,
403 West 8th Street,
Los Angeles 14, California.

Dear Mr. Egan:

There is enclosed waiver forms to be signed by

Mr. Morris Harris and Mrs. Anna Harris, each fixed in the amount of \$1,200.00, which is the deficiency tax which I am recommending in connection with the 1943 gift tax returns filed by each of them. A copy of each waiver is enclosed for your files, and an addressed return envelope which requires no postage. The deficiency tax is based upon a valuation of a 1/16th interest in the Union Manufacturing Co. at \$53,000.00, which valuation was arrived at after considering all relevant factors and elements of value, including a value for good will.

There is enclosed affidavit forms which both of the aforementioned donors need to properly execute before a notary public and submit to this office in order that the gift tax returns which they filed for 1943 be technically completed. Each return must be executed after the close of the calendar year 1943, and as filed the returns were sworn to before the close of 1943, consequently are not technically complete returns. These forms are in triplicate, but only duplicates (2) need be returned to this office.

Submission of the waivers will expedite the settlement of this case and reduce the accumulation of interest. An early receipt of the waivers and affidavits will be appreciated. Thanking you for your cooperation rendered, I remain

Very truly yours,

/s/ HUGO C. BURNS,

Internal Revenue Agent. [186]

FORM
 100-10

 THE TAX COURT OF THE U.S.
 DIV. 13 DOCKET NO. 13
 ADMITTED IN EVIDENCE

JAN 29 1948

 PETITIONERS
 EXHIBIT 12

44-38064-46

 MADE AT
 WILSON JONES CO.
 U. S. S.

DATE	ITEMS	PAID	DEBITS	DATE	ITEMS	REB	CREDITS
Feb 28	Accrued Income Tax	Q21	86,235.30	Dec 26	Balance		7,500.00
Dec 14	Cell 2.5 for 1940	CD	9,108.	Jan 31	Transf. Acc. Payable	9117	287,107.94
" 15	Trans Payable	"	5,000.	Dec 31	" 1940 Payable	Q1	3,547,019.16
" 31	Drawing Accd	Q1	9,130.38				5,549,511.10
" 31	Balance		1,805,000.38				
Jan 31	Accrued Income Tax	Q.2	49,351.04	Jan 1	Balance		471,351.04
June 4	Cell State Tax 1940	CD	23,401.32	June 20	Income tax adj.	919	5,273,019.41
" 21	"	"	16.-	Dec 31	1940 Payable	Q2	153,094.59
Sept 16	Accrued Income Tax	Q20	23,403.12				6,571,147.24
Jan 31	Drawing Accd	Q21	24,053.70				
" 31	Balance		25,111.74				
Mar 15	Cell 1940 Income Tax	Q21	25,616.90	Jan 1	Balance		3,554,447.30
Apr. 14	1944 Cell. Tax 1944	CD	355,445.30	Dec 30	1940 Payable		9,086,553.55
" 14	State Income Tax 1944	"	2,089,744.				4,633,983.55
June 13	2nd 1/2	"	9,192.06				
Sept 15	3rd 1/2	"	20,897.44				
Dec 30	Balance		2,897,444.	Jan 1	Balance		349,356.79
Mar 12	Cell 1944 Fed. Tax	CD	2,897,444.	May 11	Payable on Gross Inc.	OK	8750.
" 12	Cell 1945 " 1st 1/2	"	973,105.	Sept 30	5, Sept Tax Accd	9105	4,012,637.9
Apr. 12	1944 State Income Tax	"	15,000.	" 30	" State Income Tax	"	15,559.7
June 11	Cell 1945-2nd 1/2	"	5,661,780.	" 30	" " " "	"	5,661.73
July 10	Cell Tax Pl. 1944-47	Q47	3,399,319.4	Dec 31	1945 Payable	9140	4,012,637.9
Sept. 6	Cell 1945-3rd 1/2	CD	4,012,637.9				1,212,223.10
Dec 31	Drawing Accd	Q139	15,000.				5,264,337.09
" 31	Cell. Fed	-	4,012,637.9				
			5,264,337.09				

THE TAX COURT OF THE U.S.
 DIV. 13 DOCKET 12984
 ADMITTED IN EVIDENCE
 JAN 29 1948
 PETITIONER'S EXHIBIT 13
 RESPONSES

MADE BY
 WILSON JONES CO.
 U. S. A.

ADDRESS

BUSINESS

DATE	ITEMS	DEBIT	CREDIT
Dec 28	Accrued Income Tax	50216.48	75000
Dec 31	and Dividends	53000.47	256699.14
Dec 31	Drawing Acc.	9944.35	356025.48
" 31	Balance	465558.99	560730.62
Dec 31	Accrued Income Tax	186334.71	465558.99
Jan 30	Adv. " "	393436	153090.57
Jan 15	Billy Adams	19126.10	618630.31
Dec 31	Drawing Acc.	25005.70	
" 31	Balance	16241.97	
Mar 15	Bal. 1943 Jan. Tax	204249.71	378060.70
Apr 14	1944 Est. Tax	19755.03	998858.5
" 14	Accrued Tax	48733.45	428944.25
Jan 13	2nd 1/2	19755.03	
Sept 15	3rd 1/2	19755.03	
Dec 31	Balance	884423.46	
" 30	Drawing Acc.	96899.60	
Mar 15	Bal. 1944 Jan. Tax	378060.70	372632.19
" 15	Est. 1945 " 1st 1/2	15151.11	7271.69
Apr 15	1944 State Inc. Tax	9500.00	8755
June 10	Est. 1945-2nd 1/2	18912.05	155797
Sept 6	Est. 1945-3rd 1/2	9500.00	501201
Dec 31	Balance	210797.97	285000
" 31	Drawing Acc.	210797.97	407799.68
" 31	Balance	38120.70	520324.09
" 31	Balance	48700.00	533112.09



THE TAX COURT OF THE U.S.
DIV. 13 DOCKET/1984
ADMITTED IN EVIDENCE

JAN 29 1948

PETITIONER'S
EXHIBIT
RESPONDENT'S

14

DATE	ITEM	FILE	DEBITS	DATE	ITEM	FILE	CREDITS
Dec. 18 1943	1943 Ex Income Tax	CD	9879.79	Dec 1	1943 Prgs	Q 40	3408.70
" 31	Balance		46,074.86	Dec 2	Balance	Q 56	2,157.85
Apr. 14 1944	1944 Ex. Inc. Tax	CD	13551.70	Jan 1	1944 Prgs		46,074.86
" 14	Income Tax	"	38,104.21	Dec 30	1944 Prgs		13,883.65
June 10	2nd 1/4	"	1,354.67				59,888.51
Sept 5	State Suffix Tax	"	3,137.97				
Sept 18	Income Tax 2nd 1/4	"	4,274.27				
Dec 30	Balance		53,829.59				
Mar 12	Bel. 1944 Inc. Tax	CD	272.27	Jan 1 1945	Balance		53,829.59
" 12	Exc. 1945 - 1st 1/4	"	625.25	May 11	Prgs on Ex. Tax	CP	3,324.00
Apr 12	1944 State Inc. Tax	"	142.42	July 10	Ex. 1945 - Cap. G. 117		1,379.00
June 11	Exc. 1945 - 2nd 1/4	"	103.96	Sept 20	" State Inc. Tax	Q 120	54,920.00
Sept 6	" " 3rd "	"	166.66	" 30	" " "	"	1875.00
Dec 31	Balance		2,625.69	Dec 31	1945 Prgs	Q 160	57,007.00
			7422.08				7,891.07

625
103.96
142.42
166.66
2,625.69
7,891.07

TERMS

ADDRESS

NAME

FORM
H-2-B

THE TAX COURT OF THE U.S.
DOCKET NO. 13
DIV. ADM. IN EVIDENCE
JAN 29 1948
PETITIONER'S
EXHIBIT
DEPENDENT

DATE	ITEMS	PAY	DEBITS	DATE	ITEMS	PAY	CREDITS
1943				1943			
Nov 15	1943 Est. Income Tax	CD	9879 79	Nov 1	1/16 Loans	Dec 10	34083 70
" 31	Balance		16070 86	Dec 21	1943 Profits	Dec 10	21870 95
Apr 14	1944 Est. Tax Paid.	CD	13179 30	Jan 1	Balance		40748 6
" 14	Income Tax - State	"	39634	Dec 20	1944 Profits		129936 5
June 13	2nd " "	"	1755 87				5958 51
Sept 5	State Profits Tax	"	1809 03				
" 14	Income Tax 3rd " "	"	3014 40				
Dec 30	Balance		6327 97				
Mar 12	1944 Est. Tax	CD	5293 56				
" 12	Balance		5845 87				
Apr 12	Tax 1945 + 1st " "		207 36	Jan 1	Balance		5812 58
June 11	1944 State Income Tax	"	625 -	Profits + Tax Paid CR			5382 508
Sept 6	Est. 1945- 2nd " "	"	824 26	To A. Harris - Profits			13797
Dec 31	" " 2nd " "	"	121 68	" State Income Tax			1210 6
	Balance		1625 78	" Profits			1875 -
			2276 68	1945 Profits			5698 47
			2207 08				17883 76

PETITIONERS' EXHIBIT No. 16

[Union Manufacturing Co. Letterhead]
BALANCE SHEET—December 31, 1942

ASSETS

Petty Cash	\$ 35.49	
Union Bank & Trust Co.—Checking Act.	166,571.62	
Union Bank & Trust Co.—Payroll Acct.	100.00	
State National Bank—El Paso, Tex.....	7,797.08	
Accounts Receivable—Good	187,880.36	
Accounts Receivable—Doubtful	1,788.20	
Loans to Employees.....	106.73	
Inventory 12/21/42	538,992.70	
Machinery	40,211.68	
Furniture & Fixtures.....	694.09	
Automobile	859.80	
Stationery & Printing	400.00	
Prepaid Insurance	537.48	
		<hr/>
		\$945,975.23

LIABILITIES

Employees—Salaries, commissions, etc. \$	449.94	
Social Security—Employees	2,240.74	
Social Security—Firm	6,374.72	
		<hr/>
		\$ 9,065.40

CAPITAL

M. Harris:	\$359,705.94	
Less drawing acct.	\$28,050.00	
Less income tax 1941.....	86,238.30	
Less income tax 1940		
(add.)	92.08	114,380.38
		<hr/>
		\$245,325.56
Plus ½ 1942 profits.....	226,025.48	471,351.04
		<hr/>
		\$334,699.14
A. Harris:	\$334,699.14	
Less drawing acct.....	\$14,949.35	
Less income tax 1941.....	80,216.48	95,165.83
		<hr/>
		\$239,533.31
Plus ½ 1942 profits.....	226,025.48	465,558.79
		<hr/>
		\$945,975.23

[Endorsed]: T.C.U.S. Admitted in evidence Jan.
29, 1948. [191]

PETITIONERS' EXHIBIT No. 17

[Union Manufacturing Co. Letterhead]

BALANCE SHEET—December 31, 1943

ASSETS

Petty Cash	\$ 34.02	
Union Bank & Trust Co.—Regular Acct.	94,890.28	
Union Bank & Trust Co.—Payroll Acct.	100.00	
State National Bank of El Paso.....	7,054.83	
Accounts Receivable—Good	163,653.19	
Accounts Receivable—Doubtful	1,708.92	
Loans to Employees.....	174.14	
War Bonds	40,000.00	
Inventory of Mdse. 12/17/43.....	586,878.36	
Machinery	34,801.45	
Furniture & Fixtures.....	741.19	
Automobile	368.40	
Real Estate—El Paso (deposit).....	2,500.00	
Stationery & Printing.....	400.00	
Prepaid Insurance	1,170.49	
		<hr/>
		\$934,475.27

LIABILITIES

Due Salesmen	\$ 3,736.47	
Social Security—Employees	2,143.07	
Social Security—Firm	6,341.77	
Reserve for Income Tax—1942.....	84,887.22	
20% Withholding Taxes	11,711.02	
		<hr/>
		\$108,819.55

CAPITAL

M. Harris:	\$471,351.04	
Less 1942 Res. for Inc. Tax.....	201,283.62	
		<hr/>
	\$270,067.42	
Less adj. on 1940 State tax.....	18.06	
		<hr/>
	270,049.36	
Less Capital—Albert Harris—		
1/16 Int.	34,083.70	
		<hr/>
	\$235,965.66	
Less Drawings for year.....	41,579.45	
		<hr/>
	\$194,386.21	
Plus 7/16 1943 Profit.....	161,059.09	
		<hr/>
		\$355,445.30

A. Harris	\$465,558.79	
Less 1942 Reserve for Inc. Tax.....	190,269.06	
	<hr/>	
	\$275,289.73	
Less Capital Betty Harris—1/16 Int.	34,083.70	
	<hr/>	
	\$241,206.03	
Less drawings for year.....	24,204.42	
	<hr/>	
	\$217,001.61	
Plus 7/16 years profits.....	161,059.09	
	<hr/>	
		\$378,060.70
Albert Harris	\$ 34,083.70	
Less Estimated tax 1943.....	9,879.79	
	<hr/>	
	\$ 24,203.91	
Less 1/16 drawings.....	1,137.50	
	<hr/>	
	\$ 23,066.41	
Plus 1/16 1943 profits.....	23,008.45	
	<hr/>	
		\$ 46,074.86
Betty Harris	\$ 34,083.70	
Less Estimated tax 1943.....	9,879.79	
	<hr/>	
	\$ 24,203.91	
Less 1/16 drawings	1,137.50	
	<hr/>	
	\$ 23,066.41	
Plus 1/16 1943 profits.....	23,008.45	
	<hr/>	
		\$ 46,074.86
	<hr/>	
		\$934,475.27

[Endorsed]: T.C.U.S. Admitted in evidence Jan.
29, 1948. [193]

In the United States Circuit Court of Appeals
For the Ninth Circuit

Docket Nos. 12984, 12985
(Tax Court)

ANNA HARRIS and MORRIS HARRIS,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR REVIEW OF DECISION OF
THE TAX COURT OF THE UNITED STATES

To the Honorable Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:

Anna Harris and Morris Harris, petitioners in
the above entitled cases which were consolidated
for trial below, hereby petition this court to re-
view the decision of the Tax Court of the United
States heretofore entered in said proceeding on
May 12, 1848. Petitioners respectfully represent:

I.

This petition is filed pursuant to Internal Reve-
nue Code sections 1141 and 1142, 26 U.S.C.A., sec-
tions 1141 and 1142. [194]

II.

Nature of Controversy

The present controversy relates to the proper
determination of petitioners' federal income and

victory taxes for the calendar year 1943 and federal income taxes for the calendar year 1944.

Respondent determined deficiencies to be due from petitioners for the calendar years 1943 and 1944 as follows:

Anna Harris:

1943	\$5,662.73
1944	18,136.67

Morris Harris:

1943	\$ 6,036.87
1944	18,693.10

The Tax Court of the United States, by its said decision, sustained respondent in his determinations and petitioners hereby petition for a review of said decision of the Tax Court of the United States.

III.

Venue

Petitioners filed their respective separate federal income tax returns for the calendar years 1943 and 1944 with the Collector of Internal Revenue for the Sixth District of California. Accordingly, petitioners are petitioning for a review of the said decision of the Tax Court of the United States by this Circuit Court of Appeals for the Ninth Circuit.

Wherefore, your petitioners pray that this court review the said decision of the Tax Court of the United States, [195] reverse the said decision of said Tax Court, and direct entry of a decision by

said Tax Court in favor of petitioners and each of them, determining that no deficiencies in federal income or victory taxes for the calendar years 1943 and 1944 are due from the petitioners or either of them.

Dated July 29, 1948.

Respectfully submitted,

/s/ DANA LATHAM,
Attorney for Petitioners.

(Duly Verified.)

[Endorsed]: T.C.U.S. Aug. 4, 1948. [196]

[Title of U. S. Court of Appeals and Causes.]

NOTICE OF FILING OF PETITION
FOR REVIEW

To the Commissioner of Internal Revenue, Washington, D. C.:

You are hereby notified that Anna Harris and Morris Harris, petitioners in the above entitled proceeding in the Tax Court of the United States is petitioning the United States Circuit Court of Appeals for the Ninth Circuit to Review the decision of said Tax Court heretofore rendered in

the above-entitled Tax Court case on May 12, 1948. The petition for review, copy of which is attached hereto, and this notice of filing of petition for review are hereby served upon you.

Dated July 29, 1948.

/s/ DANA LATHAM,
Attorneys for Petitioners.

(Acknowledgment of Service.)

[Endorsed]: T.C.U.S. Filed Aug. 4, 1948. [198]

[Title of U. S. Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD
ON APPEAL AND STATEMENT OF POINTS

To Victor S. Mersch, Clerk of the Tax Court of
the United States, Washington, D. C.:

Petitioners in the above-entitled consolidated proceedings hereby designate the following portions of the record, proceedings, and evidence before the Tax Court of the United States to be contained in the record on review before the Circuit Court of Appeals for the Ninth Circuit:

- (1) Docket entries.
- (2) Petition and amended petition of petitioner Anna Harris (Docket No. 12984).
- (3) Petition and amended petition of petitioner Morris Harris (Docket No. 12985).
- (4) Answer to petition and amended petition of [201] petitioner Anna Harris (Docket No. 12984).

(5) Answer to petition and amended petition of petitioner Morris Harris (Docket No. 12985).

(6) Findings of fact and opinion of the Tax Court.

(7) Decision of the Tax Court, if separate and distinct from (6) above.

(8) The reporter's transcript of proceedings before the Tax Court.

(9) The following exhibits introduced in evidence by petitioners at the hearing before the Tax Court:

1. Petitioners' Exhibit "1".
2. Petitioners' Exhibit "2".
3. Petitioners' Exhibit "3".
4. Petitioners' Exhibit "5".
5. Petitioners' Exhibit "6".
6. Petitioners' Exhibit "7".
7. Petitioners' Exhibit "8".
8. Petitioners' Exhibit "9."
9. Petitioners' Exhibit "10".
10. Petitioners' Exhibit "11".
11. Petitioners' Exhibit "12".
12. Petitioners' Exhibit "13".
13. Petitioners' Exhibit "14".
14. Petitioners' Exhibit "15".
15. Petitioners' Exhibit "16".
16. Petitioners' Exhibit "17".

[202]

(10) The petition for review of decision of the Tax Court and notice of filing of petition for review, together with proof of service of said petition and said notice of filing petition.

(11) This designation of contents of record on appeal and statement of points and the notice of filing thereof, together with proof of service of said designation and notice.

STATEMENT OF POINTS ON WHICH PETITIONER INTENDS TO RELY

(1) The Tax Court erred in entering decisions for respondent.

(2) The Tax Court erred in not entering decisions for petitioners and each of them.

(3) The Tax Court erred in failing to find or conclude that there were no deficiencies in income and victory taxes due from petitioners or either of them for the calendar years 1943 and 1944.

(4) The Tax Court erred in failing to find or conclude that there was, as of January 1, 1943, a completed gift in praesenti to petitioners' son Albert of a one-sixteenth interest in petitioners' business, which vested him with complete dominion and control over an interest in and earnings of said business. [203]

(5) The Tax Court erred in failing to find or conclude that there was, as of January 1, 1943, a completed gift in praesenti to petitioners' daughter, Betty of a one-sixteenth interest in petitioners' business, which vested her with complete dominion and control over an interest in and earnings of said business.

(6) The Tax Court erred in failing to find or conclude that petitioners' son Albert was a bona

fide partner with petitioners and Betty Harris throughout the calendar years 1943 and 1944.

(7) The Tax Court erred in failing to find or conclude that petitioners' daughter Betty was a bona fide partner with petitioners and Albert Harris throughout the calendar years 1943 and 1944.

(8) The Tax Court erred in failing to find or conclude that petitioners' son Albert was the owner of and taxable on his share of the income of the partnership referred to in (6) and (7) above for the calendar years 1943 and 1944 as shown on petitioners' Exhibits "5", "6", and "14".

(9) The Tax Court erred in failing to find or conclude that petitioners' daughter Betty was the owner of and taxable on her share of the income of the partnership referred to in (6) and (7) above for the calendar years 1943 and 1944 as shown on petitioners' Exhibits "5", "6", and "15".

(10) The Tax Court erred in finding or concluding that petitioners were each taxable on 50% of the income of the [204] partnership referred to in (6) and (7) above for the calendar years 1943 and 1944.

(11) The Tax Court erred in finding or concluding that the said partnership had two members only, Anna and Morris Harris, during the calendar years 1943 and 1944, and in failing to find or conclude that said partnership had four members, Anna, Morris, Albert, and Betty Harris, during said years.

(12) Assuming, but not conceding, that the Tax

Court did not err in finding or concluding that Albert and Betty Harris were not bona fide partners with petitioners during the calendar years 1943 and 1944, then the Tax Court erred in failing to find or conclude that the said Albert and Betty Harris were each the owners of their respective interests in the capital of the business and the owners of and taxable on the income of said business to the extent attributable to their said respective interests in said capital and in failing and refusing to fix and determine the amount of income so attributable to said capital interests.

(13) The Tax Court erred in failing to find or conclude that the \$25,256.18 California income tax paid by the petitioner Anna Harris during the calendar year 1943 was deductible by said petitioner in computing victory tax net income for said year.

(14) The Tax Court erred in failing to find or conclude that the \$26,746.65 California income tax paid by the petitioner Morris Harris during the calendar year 1943 was [205] deductible by said petitioner in computing victory tax net income for said year.

Dated August 4, 1948.

Respectfully submitted,

/s/ DANA LATHAM,

/s/ D. WEBSTER EGAN,

Attorneys for Petitioners.

[Endorsed]: T.C.U.S. Filed Aug. 6, 1948. [206]

[Title of U. S. Court of Appeals and Cause.]

NOTICE OF FILING OF DESIGNATION OF
CONTENTS OF RECORD ON APPEAL
AND STATEMENT OF POINTS

To the Commissioner of Internal Revenue, Wash-
ington, D. C.:

You are hereby notified that Anna Harris and Morris Harris, petitioners in the above-entitled proceeding in the Tax Court of the United States, are filing with the Clerk of the Tax Court petitioners' designation of contents of record on appeal and statement of points. The said designation of contents of record on appeal and statement of points, a copy of which is attached hereto, together with this notice of filing of same, are hereby served upon you.

Dated August 4, 1948.

/s/ DANA LATHAM,

/s/ D. WEBSTER EGAN,

Attorneys for Petitioners.

(Affidavit of Service attached.)

[Endorsed]: Filed Aug. 6, 1948.

[207]

[Title of U. S. Court of Appeals and Cause.]

DESIGNATION OF ADDITIONAL PORTIONS
OF RECORD

To the Clerk of The Tax Court of the United
States:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct, of the following additional documents and records in the above-entitled causes in connection with the petition for review by the said Circuit Court of Appeals for the Ninth Circuit, heretofore filed by the taxpayers, petitioners herein:

1. Petitioners' Exhibit 4.

/s/ THERON L. CAUDLE,
Assistant Attorney General.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.
Attorneys for Respondent on
Review.

(Acknowledgment of Service attached.)

[Endorsed]: T.C.U.S. Filed Aug. 24, 1948. [209]

[Title of Tax Court and Cause.]

CERTIFICATE

I, Victor S. Mersch, clerk of The Tax Court of the United States do hereby certify that the foregoing pages, 1 to 209, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praeceptum in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 30th day of September, 1948.

(Seal) /s/ VICTOR S. MERSCH,
Clerk, The Tax Court of the United States.

[Endorsed]: No. 12060. United States Court of Appeals for the Ninth Circuit. Anna Harris and Morris Harris, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed October 11, 1948.

 /s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

In the United States Court of Appeals for the
Ninth Circuit

Docket No. 12060

ANNA HARRIS and MORRIS HARRIS,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STATEMENTS OF POINTS AND DESIGNA-
TION OF PARTS OF RECORD TO BE
PRINTED

To the Clerk of the United States Court of Appeals
for the Ninth Circuit:

I.

STATEMENT OF POINTS

Petitioners respectfully state that upon the hearing on their petition for review herein, petitioners intend to rely upon all of the points specified in their "Designation of Contents of Record on Appeal and Statement of Points" heretofore filed with the Clerk of the Tax Court of the United States, which points are incorporated herein by reference.

II.

DESIGNATION OF PARTS OF RECORD
TO BE PRINTED

Petitioners respectfully submit that all of the record on review, as certified to you, with the exception of Petitioners' Exhibit 4 certification of which was requested by respondent, will be necessary for the consideration of the points upon which petitioners intend to rely. Accordingly, petitioners respectfully request you to have printed the entire record on review except Petitioners' Exhibit 4.

/s/ DANA LATHAM,

/s/ HENRY C. DIEHL,

/s/ D. WEBSTER EGAN,

Attorneys for Petitioners.

(Affidavit of Service attached.)

[Endorsed]: Filed October 26, 1948. Paul P. O'Brien, Clerk.

No. 12060

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ANNA HARRIS and MORRIS HARRIS,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

DANA LATHAM,

HENRY C. DIEHL,

1112 Title Guarantee Building, Los Angeles 13,

D. WEBSTER EGAN,

320 Garfield Building, Los Angeles 14,

Attorneys for Petitioners.

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No. 12060

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ANNA HARRIS and MORRIS HARRIS,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

Jurisdiction.

This petition for review involves deficiencies in Federal income and victory taxes for the years 1943 and 1944 in the total amount of \$23,799.40 as to petitioner Anna Harris [Tr. 71], and \$24,728.97 as to petitioner Morris Harris. [Tr. 72.] The cases of the two petitioners involve identical issues and were consolidated for hearing before The Tax Court of the United States, hereinafter referred to as the "Tax Court." The decisions of the Tax Court determining said deficiencies were entered May 12, 1948. [Tr. 71-72.]

This petition for review was filed August 4, 1948 [Tr. 164] pursuant to the provisions of sections 1141 and 1142 of the Internal Revenue Code, 26 U. S. C. A., sections 1141 and 1142.

Opinion Below.

The only previous opinion rendered in this cause is the opinion of the Tax Court [Tr. 51-71] reported in 10 T. C., No. 109.

Issues Involved.

There are two issues involved:

(1) Did respondent err in ignoring a partnership consisting of petitioners and their children wherein assets were owned and profits and losses were divided on the following basis:

Morris Harris	7/16ths
Anna Harris	7/16ths
Albert P. Harris	1/16th
Betty Harris	1/16th

and in taxing all of said partnership income for the years in question equally to petitioners.

(2) In determining their 1943 victory tax liability, are petitioners entitled to deduct all or any part of the California State income tax paid by them during said year 1943?

Statutes and Regulations Involved.

Internal Revenue Code (26 U. S. C. A.)

“SEC. 22. GROSS INCOME.

“(a) General Definition.—‘Gross income’ includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such President and judges are hereby amended accordingly. In the case of judges of courts of the United States who took office on or before June 6, 1932, the compensation received as such shall be included in gross income.”

“SEC. 181. PARTNERSHIP NOT TAXABLE.

“Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.”

“SEC. 182. TAX OF PARTNERS.

“In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

“(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).”

“SEC. 451. VICTORY TAX NET INCOME.

“(a) Definition.—The term ‘victory tax net income’ . . . means . . . the gross income . . . minus the sum of the following deductions:

* * * * *

(3) Taxes. Amounts allowable as a deduction by section 23(c), to the extent such amounts are paid or incurred in connection with the carrying on of a trade or business, or in connection with property used in the trade or business, or in connection with property held for the production of income.”

“SEC. 23(c)

“Taxes Generally—

“(1) Allowance in general.—Taxes paid or accrued within the taxable year, except—

“(A) Federal income taxes;

“(B) war-profits and excess profits taxes imposed by Title II of the Revenue Act of 1917, Title III of the Revenue Act of 1918, Title III of the Revenue Act of 1921, section 216 of the National Industrial Recovery Act, section 702 of the Revenue Act of

1934, or Sub-chapter E of Chapter 2, or by any such provisions as amended or supplemented;

“(C) income, war-profits and excess-profits taxes imposed by the authority of any foreign country or possession of the United States, if the taxpayer chooses to take to any extent the benefits of section 131;

“(D) estate, inheritance, legacy, succession, and gift taxes;

“(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed, but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; and

“(F) Federal import duties, and Federal excise and stamp taxes (not described in subparagraph (A), (B), (D), or (E)), but this subsection shall not prevent such duties and taxes from being deducted under subsection (a).”

Regulations 111.

“REG. 111, SEC. 29.451-2.

“(2) Taxes.—Taxes deductible under 23(c) allowable for Victory Tax purposes if, and only if, paid or incurred—

“(i) in connection with the carrying on of a trade or business;

“(ii) in connection with property used therein; or

“(iii) in connection with property held for production of income.”

Statement of Facts.

This proceeding was submitted to the Tax Court on the pleadings, oral testimony offered by the petitioners, and exhibits introduced in evidence at the hearing. *The respondent introduced no evidence.*

The facts here involved may be summarized as follows:

(1) The Union Manufacturing Company, the principal place of business of which is now located in Los Angeles, California, was founded in 1909. [Tr. 82.] It was and is engaged in the business of manufacturing men's work and sport clothes. [Tr. 83.] For a period of time and in particular during the war years, its business was substantial. [Tr. 109-111.]

(2) Union Manufacturing Company originally consisted of a partnership between one of the petitioners herein, Morris Harris, and Mr. Pinkert, the father of the other petitioner, Anna Harris. [Tr. 82.] The petitioner Anna Harris worked part time in the business from the time she attained high school age. [Tr. 82.] After she finished high school she gave her entire time to the partnership conducted by Morris Harris and her father, performing responsible functions. [Tr. 82-83.]

(3) Petitioners were married in 1919 [Tr. 82] and petitioner Anna Harris continued to work full time in the business until the birth of her first child. Even after the children were born she gave a substantial part of her time to the business, coming regularly to the office and performing important and vital functions. [Tr. 83-84.]

(4) The partnership between petitioner Morris Harris and Mr. Pinkert was terminated at the end of 1923. [Tr. 83.] A new equal partnership was then formed be-

tween the two petitioners herein which began operations January 1, 1924. [Tr. 83-84.] The partnership agreement is in evidence as Petitioners' Exhibit 3. [Tr. 137-138.] After the formation of said partnership petitioner Anna Harris continued to perform vital services for the enterprise. [Tr. 84.]

(5) Two children were born to the petitioners herein, Albert P. Harris, born June 14, 1923, and Betty Harris, born September 22, 1926. [Tr. 84.] The partnership agreement of 1924 expired according to its terms at the end of ten years. It was renewed by another document in writing dated April 1, 1937. [Tr. 85, Pet. Ex. 4.] This agreement remained in effect until January 1, 1943 when it was supplanted by a partnership agreement between the two petitioners and their two children to be hereinafter referred to. [Tr. 85.]

The existence of an equal partnership between petitioners herein up to January 1, 1943 was recognized by the Tax Court in its opinion below. [Tr. 51.]

(6) Albert F. Harris early took a real interest in the business and always intended to become an active member of the enterprise. [Tr. 86 and 116-117.] When petitioners were considering the sale of the business in 1937, Albert expressed opposition because he had always hoped to join his parents in its operation. [Tr. 86.] As a result the proposed sale was abandoned. [Tr. 86.]

(7) Albert worked in the business after school and during vacation periods while in high school. [Tr. 91 and 115-116.] He finished high school in June, 1941, and requested permission to immediately enter the business without attending college. With difficulty petitioners persuaded him to enter college on the representation that he

would be of more value to the business with further schooling. [Tr. 86 and 116.]

(8) In accordance with his understanding with petitioners, Albert entered the University of Virginia in the fall of 1941, after having worked during the summer vacation in the business. During this first school year he took the general college course. [Tr. 86 and 115.]

(9) Upon his return to Los Angeles in June of 1942 Albert again asked for permission to enter the business full time. During the summer of 1942 he worked full time in various departments of the business, performing substantial services, and at night attended the University of Southern California where he took specialized courses dealing with textiles. [Tr. 87 and 116-117.] During said summer the formation of a partnership between petitioners and Albert was discussed. In connection therewith petitioners consulted their attorney. [Tr. 87-88.]

(10) In the fall of 1942 petitioners, by promising Albert an interest in the business, were able to persuade him to continue his specialized training in textiles begun at the University of Southern California in the summer of 1942. Accordingly, in September, 1942, Albert entered the Textile School of the University of North Carolina, at Raleigh, North Carolina. [Tr. 87 and 117.]

(11) During the Christmas holidays of 1942 Albert again returned to Los Angeles and at that time the partnership between petitioners herein, Albert and Betty was definitely agreed upon. Albert received a *sixteenth* interest in assets and profits and losses of the business, and Betty the same. [Tr. 87-88 and 117-118.] Betty was included at that time in order to avoid the appearance of favoritism and with the hope that she might eventually take an active part in the business. [Tr. 88.]

(12) The partnership formed at Christmas 1942 was not reduced to writing, the parties' attorneys having advised them that a writing was unnecessary. [Tr. 89.] The agreement of the parties with respect to the partnership, however, was clear, definite, and unequivocal. [Tr. 88-89, 117-118, and 120.] There was no restriction as to the powers, rights of withdrawal, etc. of any of the partners [Tr. 89.] *In connection with the formation of said partnership income taxes were not considered or discussed.* [Tr. 106.]

(13) At the conclusion of the Christmas holidays his partners requested Albert to return to school, believing that he as a partner could be of best use to the partnership by increasing his specialized knowledge of textiles and their manufacture. [Tr. 116-118.]

(14) In the meantime in anticipation of the draft Albert had enlisted in the United States armed forces and was expecting a call to active duty after he returned to college. [Tr. 92 and 117.] He was called into active service in April, 1943 [Tr. 92 and 118] and remained in active service until January, 1946. Upon his discharge he went immediately into the business and has devoted his full time continuously thereto, performing at all times responsible functions. [Tr. 92-93 and 119.]

(15) As required by law, petitioner Anna Harris filed a gift tax return, Form 709, showing the gift to Albert during 1943 of a one-sixteenth interest in the assets of Union Manufacturing Company. [Tr. 94 and 149-151.] A donee gift tax return, Form 710, was duly filed by Albert covering said gift. [Tr. 95 and 151.] Likewise Morris Harris filed a gift tax return, Form 709, showing the gift to Betty during 1943 of a one-sixteenth interest in the assets of Union Manufacturing Company. [Tr.

95 and 152.] A donee gift tax return, Form 710, was duly filed by Betty covering said gift. [Tr. 95 and 152.] The returns referred to are in evidence as Petitioners' Exhibits 7, 8, 9 and 10. [Tr. 149-152.]

(16) Respondent audited said gift tax returns herein referred to and by letter dated September 25, 1945, increased the values placed upon the gifts made by petitioners herein and demanded and received from petitioners additional gift taxes. [Tr. 96 and 152-153.]

(17) Capital accounts were set up on the books of Union Manufacturing Company showing the interests in the partnership assets of the four partners, including Albert and Betty. Petitioners' Exhibits 12, 13, 14 and 15 are the ledger sheets showing the capital accounts of Morris, Anna, Albert and Betty Harris, respectively. [Tr. 100-101 and 154-157.] In said ledger sheets it is inadvertently shown that Albert was the donee of his father and Betty the donee of her mother [Tr. 127-128], although in fact and as shown by the gift tax returns, Albert was the donee of his mother and Betty the donee of her father. [Tr. 94-95.] The error is immaterial, however, as the amounts involved were identical. [Tr. 128.]

(18) According to page 40 of the General Journal of Union Manufacturing Company the entries opening new capital accounts for Albert and Betty and charging the capital accounts of petitioners herein were made September 16, 1943, as of January 1, 1943. [Tr. 102.] The delay in making appropriate entries was due to an oversight

on the part of the interested parties, each believing that someone else had attended to it. [Tr. 103.]

(19) At the end of each of the years 1943 and 1944 one-sixteenth of the earnings of the business was credited to the capital accounts of Albert and Betty, respectively. Their withdrawals (for Federal income taxes) were charged to their capital accounts. [Tr. 128-129 and 156-157.]

(20) Federal partnership returns, Form 1065, were filed for each of the calendar years 1943 and 1944 for Union Manufacturing Company. These returns showed Albert P. and Betty Harris as partners with the petitioners herein in the following proportions:

Morris Harris	7/16ths	
Anna Harris	7/16ths	
Albert P. Harris	1/16th	
Betty Harris	1/16th	[Tr. 93-94.]

Said returns are in evidence as Petitioners' Exhibits 5 and 6. [Tr. 139-148.]

(21) In auditing the returns of petitioners herein for the calendar years 1943 and 1944 respondent ignored the partnership formed January 1, 1943, and charged to petitioners herein equally the income belonging to and reported by Albert P. and Betty Harris.

(22) During the calendar year 1943 petitioner Morris Harris paid to the State of California personal income tax in the amount of \$26,746.65. [Tr. 80.] The return showing said tax is in evidence as Petitioners' Exhibit 1. [Tr. 130-134.] During said year petitioner Anna Harris

paid to the State of California personal income tax in the amount of \$25,256.18. [Tr. 81.] The return showing said tax is in evidence as Petitioners' Exhibit 2. [Tr. 134-136.] As shown by said exhibits, substantially all of said tax resulted from the inclusion in petitioners' taxable income of the income accruing to them from the Union Manufacturing Company.

(23) Petitioners in computing their liability for Victory Tax for the calendar year 1943 deducted the amounts paid to the State of California as personal income taxes as set forth in the preceding paragraph hereof. Respondent disallowed said amounts as deductions in computing said Victory Tax.

(24) The facts as found by the Tax Court [Tr. 52-59] are at variance with those stated hereinabove only in the lower court's conclusion that (1) neither of the children contributed any capital of their own [Tr. 58]; (2) Albert's services prior to 1943 were not substantial [Tr. 58]; (3) neither of the children withdrew any amounts from the partnership during 1943 and 1944 [Tr. 58]; (4) no new and bona fide partnership was formed in 1943 [Tr. 59]; and (5) petitioners Anna and Morris Harris were the only partners during 1943 and 1944. [Tr. 59.] The Tax Court also failed to find that in returning to textile school in January, 1943 at the request of his partners *Albert was, in fact, performing vital services for the partnership.*

(25) The Tax Court sustained the respondent on both issues as to both petitioners. The petition for review herein followed.

Specification of Errors.

(1) The Tax Court in its Findings of Fact made no finding as to whether or not completed gifts of interests in the partnership theretofore conducted by petitioners were made by petitioners to their two children.

If the Tax Court's opinion is to be read as containing a finding that no such valid gifts were made, then such finding is totally without support in the evidence and the Tax Court erred in that particular.

(2) The Tax Court erred in failing to find or conclude that there was in existence throughout the years 1943 and 1944 a bona fide partnership consisting of Anna Harris, Morris Harris, Albert Harris, and Betty Harris, and that said partnership should be recognized for Federal income tax purposes.

(3) The Tax Court erred in failing to find or conclude that the California income taxes paid by the petitioners during the year 1943 were deductible by said petitioners in computing their respective victory tax net incomes for said year.

Summary of Argument.

The argument herein will, of course, be divided into two parts, the first relating to the partnership issue and the second to deductibility of California income taxes in computing victory tax net income. The first applies to both years involved—1943 and 1944; the second applies only to the year 1943.

(1) On the first issue petitioners contend as follows:

(a) Bona fide gifts of interests in the partnership were in fact made by petitioners to their two children effective January 1, 1943.

(b) The partnership consisting of petitioners and said two children must be recognized for Federal Income tax purposes because said partnership was not formed for the purpose of dividing family income and thus reducing the income taxes of the family group but was a bona fide business arrangement whereby the parties really and truly intended to carry on business together as partners within the rationale of the decisions of the Supreme Court in the cases of *Commissioner v. Tower*, 327 U. S. 280, 66 S. Ct. 532, and *Lusthaus v. Commissioner*, 327 U. S. 293, 66 S. Ct. 539, to be hereinafter referred to.

It will be shown that it is the *intention of the parties* which is controlling, and not the presence or absence of any particular element such as the contribution of capital or the rendering of vital services. It will be pointed out that the *record* clearly reveals the bona fides of the partnership and *contains no evidence in support of the Tax Court's conclusion that there was no valid partnership for Federal income tax purposes.*

(2) On the second issue, it is petitioners' contention that the clear language of the statutes permits the deduction of California income taxes in computing victory tax net income. The only requirement of the statute, as set forth above, is that the taxes were paid or incurred in connection with the carrying on of a trade or business. The California income taxes paid by the petitioners were paid on and by reason of income earned in their business, hence were paid in connection with the carrying on of that business and are deductible in arriving at victory tax net income.

Outline of Argument.

A. ON JANUARY 1, 1943 VALID GIFTS OF INTERESTS IN THE THEN EXISTING PARTNERSHIP OF UNION MANUFACTURING COMPANY WERE MADE BY THE THEN PARTNERS, PETITIONERS HEREIN, TO THEIR TWO CHILDREN.

B. THE PARTNERSHIP EFFECTIVE JANUARY 1, 1943, BETWEEN PETITIONERS HEREIN AND ALBERT AND BETTY HARRIS WAS VALID AND SHOULD BE RECOGNIZED FOR FEDERAL INCOME TAX PURPOSES.

C. INCOME TAXES PAID TO THE STATE OF CALIFORNIA DURING THE YEAR 1943 ARE DEDUCTIBLE IN DETERMINING PETITIONERS' RESPECTIVE VICTORY TAX NET INCOMES FOR THAT YEAR.

ARGUMENT.

A. On January 1, 1943 Valid Gifts of Interests in the Then Existing Partnership of Union Manufacturing Company Were Made by the Then Partners, Petitioners Herein, to Their Two Children.

Petitioners in the "Statement of Facts" heretofore set forth in this brief specifically enumerated the circumstances connected with the gifts by petitioners on January 1, 1943 of a one-sixteenth interest in the assets and business of the Union Manufacturing Company to petitioners' two children.

The Tax Court in its Findings of Fact makes no specific finding with respect to the validity of said gifts. In its Opinion, which is at best confused, the Tax Court intimates that bona fide gifts of interests in said partnership may not have been made by petitioners to their two children.

It is respectfully submitted that the Tax Court erred in not making a specific finding on this point in its Findings of Fact.

On the other hand, if the Court's Opinion (as opposed to its Findings of Fact) is to be deemed to constitute a finding against petitioners on this point, then the Tax Court erred in making any such finding as *there is no evidence of any kind or nature in the record to support any such conclusion.*

The facts as clearly and unequivocally established by the record show the following:

(1) Both petitioners testified without contradiction that gifts of an interest in the assets and business of the partnership were made by them to their two children as of January 1, 1943.

(2) Federal gift tax returns both in behalf of the donors and the donees showing such gifts were filed with respondent herein and duly audited by him.

(3) The values of said gifts at the date thereof, January 1, 1943, were questioned by respondent upon his audit thereof and were substantially increased. As a result, respondent demanded and collected from petitioners additional gift taxes on account of said gifts.

(4) Proper and appropriate entries indicating the ownership by the children of a one-sixteenth interest each in the assets of the business as of January 1, 1943 were duly made on the books of the partnership. The income taxes of the two children were paid during each of the years in question from their interest in the assets of the business and their capital accounts were charged accordingly.

(5) Appropriate Federal income tax returns were filed for each of the years in question showing that the children were partners in said enterprise and in truth and fact owned an interest in the assets and business as indicated by the gift tax returns filed by petitioners herein.

(6) The children on their individual returns for the years in controversy included and paid tax on their distributable shares of said partnership income.

(7) The parties testified without equivocation that there was no restriction on the powers, rights of withdrawal, etc. of any of the partners, including specifically petitioners' children.

(8) There is absolutely not a shred of evidence in the record to justify a finding that bona fide gifts of interests in the business and assets of the Union

Manufacturing Company were not made by petitioners herein as of January 1, 1943 to their two children.

As a matter of fact, the Tax Court does not even attempt to justify its intimation that no completed gift was made. Certain comments of the Court [Tr. 66] are worthy of note:

(1) The Tax Court states that there was no written partnership agreement. It is too clear to require comment that the absence of a written agreement is not evidence that no completed gifts of partnership interests were made.

(2) It is stated that the "alleged verbal agreement was a loose one." There is absolutely no basis for any such statement. The parties testified that each child acquired a one-sixteenth interest in the assets and profits and losses of the business. That is clearly sufficient to establish a partnership. As a matter of fact, it is well known that most partners go no further in specifying their rights and duties one to the other.

(3) The Tax Court states that the "partnership books were not closed." There is absolutely nothing in the record to justify any such gratuitous statement. As a matter of fact, the evidence shows exactly the contrary, and above all, that the books of account of the partnership and the parties were at all times meticulously maintained.

It is true that the initial book entries setting up the children's accounts on the books of the partnership were not made until September 16, 1943 and then as of January 1, 1943. The parties testified, however, that that was due to an oversight and to nothing more in that the

interested parties each thought that some one else had attended to it.

It is respectfully submitted that if the Tax Court shall be deemed to have found as a matter of fact or law that no completed gifts were made by petitioners to their children of interests in the partnership in question, that such finding was arbitrary and totally without support in the evidence.

B. The Partnership Effective January 1, 1943, Between Petitioners Herein and Albert and Betty Harris Was Valid and Should Be Recognized for Federal Income Tax Purposes.

It would unduly prolong this brief to enter upon a detailed discussion of the many so-called family partnership cases. This argument will, therefore, be limited to a discussion of a few cases which we deem to be significant.

At the head of a long line of cases from the various courts stand *Commissioner v. Tower*, 327 U. S. 280, 66 S. Ct. 532, and *Lusthaus v. Commissioner*, 327 U. S. 293, 66 S. Ct. 539. These are the cases which expound the basic rule which the courts in all subsequent cases have attempted to apply to the facts before them. The rule may be very simply stated by the following quotation from the *Tower* decision:

“When the existence of an alleged partnership arrangement is challenged by outsiders, the question arises whether the partners really and truly intended to join together for the purpose of carrying on business and sharing in the profits or losses or both.”

In the latter part of its decision in the *Tower* case, the Supreme Court acknowledged that a wife might, under

proper circumstances, he recognized as a bona fide partner. The court then enumerated certain tests, the absence of all of which "the Tax Court may properly take . . . into consideration in determining whether the partnership is real within the meaning of the federal revenue laws." The tests so enumerated are a share in the management and control of the business, the rendering of vital additional services, or the contribution of capital originating with her.

Ignoring the statement of the Supreme Court that the factors referred to above were merely *some* of the facts to be considered in arriving at an ultimate decision, the Tax Court, in a long line of cases decided subsequent to the *Tower* and *Lusthaus* cases, seized upon the presence or absence of the three above mentioned factors as *conclusive* in determining the validity of the partnership under attack. No attempt was made to independently determine the intent of the parties. As will be hereinafter pointed out, it has been but very recently that the Tax Court has apparently returned to the true test of intent.

The Federal District Courts and Circuit Courts of Appeal, however, have almost without exception read the *Tower* and *Lusthaus* cases as prescribing the rule of *intent*. Accordingly said courts have refused to apply blindly as conclusive tests the contribution of independent capital not originating with the parent and the performance of alleged vital services.

In three district court cases tried before juries, the juries were instructed that the question was whether the partnership was a genuine, bona fide, good faith organization, and whether the parties really and truly intended to carry on business as partners. The juries were instructed

that the presence or absence of a contribution of capital, a share in management, and vital services rendered by the questioned partner were merely elements to be considered in answering the ultimate question. In all three cases the juries found for the taxpayers. The cases are *Knott v. Allen*, U. S. D. C., M. D., Georgia (January, 1947), reported at paragraph 72,414 P-H Fed. 1947, affirmed by C. C. A. 5 in *Allen v. Knott*, 166 F. 2d 798; *Mallory, Jr., v. Allen*, U. S. D. C., M. D., Georgia (November, 1947), reported at paragraph 72,615 P-H Fed. 1947; and *Hager v. Kavanagh*, U. S. D. C., W. D., Michigan (December, 1947), reported at paragraph 72,462 P-H Fed. 1948.

Similarly, in *Cooke v. Glenn*, U. S. D. C., W. D., Kentucky (June, 1948), reported at paragraph 72,551 P-H Fed. 1948, the court, sitting without a jury, found for the taxpayer, based upon "the intention of the parties and their good faith in joining together for the purpose of carrying on business and sharing in the profit or loss."

Various of the circuit courts have also taken the same view as to the true meaning of the Supreme Court's pronouncements in the *Tower* and *Lusthaus* cases. A number of reversals of the Tax Court have resulted. Some of these cases merit a brief discussion.

In *Lawton v. Commissioner*, 164 F. 2d 380 (C. C. A. 6, November, 1947), the same judge who heard the instant controversy as a judge of the Tax Court had concluded that no bona fide partnership existed, in spite of the uncontradicted evidence of the petitioners that a partnership was intended and in fact existed. The Circuit Court reversed, stating that the undisputed and uncontradicted evidence of the parties may not be arbitrarily disregarded by the fact finder. The appellate court further gave im-

portance to the fact that the business was “a coordinated family enterprise” started by the father and mother “into which were integrated the sons and daughters as they came from school and college, to the extent that their training and abilities became useful.” In short, the parties really and truly intended to do business as partners, regardless of capital contributions or the nature and extent of services rendered.

The Tax Court was again reversed in *Culbertson v. Commissioner*, 168 F. 2d 979 (C. C. A. 5, June, 1948; cert. granted, December, 1948), where the disputed partners had not contributed their own capital and had performed no services during the year in question because either in school or in military service. The opinion contains such an illuminating discussion of the principles applicable to these cases that it is deemed appropriate to quote extensively therefrom:

“It was the purpose and intent of all the parties to form an actual, real, and bona fide partnership between Culbertson and his four sons, with the full expectation and purpose that the boys would, in the future, contribute their time and services to the partnership. *We do not consider that it is illegal, income-tax-wise or otherwise, for a partnership to be formed in consideration, or contemplation, of services rendered, or to be rendered, by the partners. The fact that the boys were called into the military service by the United States, as well as the fact that some of them had not, during the tax period, completed their education so as to devote their full time and attention to the partnership is in no wise indicative that the partnership was formed for the purpose of dividing the family income, or for the purpose of income tax savings.* The failure by a partner to render service

to the partnership or to contribute capital originating in him, is, after all, but a circumstance to be considered in determining the reality or actuality of an alleged family partnership. The failure to do either is not a condition precedent.” (*Italics supplied.*)

* * * * *

“In the cases of *Commissioner v. Tower*, 327 U. S. 280 (66 S. Ct. 532, 34 A. F. T. R. 799); and *Lusthaus v. Commissioner*, 327 U. S. 293 (66 S. Ct. 539, 34 A. F. T. R. 806), the court determined that the arrangements there were mere devices entered into for income tax savings and purposes and not for the benefit of the partnership. To conclude in this case that the plan and purpose of an aging father to enlist the interest and services of his four ranch-reared, experienced, and stalwart sons in the carrying on of his and his partner’s life work was not for the partnership’s benefit seems to require the exaltation of suspicion over the realities to an extent that the exigencies of the times for tax collection neither deserve nor demand.”

* * * * *

“It seems that out of the cases of *Lusthaus v. Commissioner*, *supra*, and *Commissioner v. Tower*, *supra*—which cases were properly decided on their peculiar facts—a concept has been born and is carefully nurtured by the tax collecting agencies that no partnership is valid—*income-tax-wise*—between members of a family unless the members of the family coming into the partnership actually contribute money or had actually, theretofore, rendered services. Neither statute, common sense, nor impelling precedent requires the holding that a partner must contribute capital or render services to the partnership prior to the time that he is taken into it.

“These tests are equally effective whether the capital and the services are presently contributed and rendered or are later to be contributed or to be rendered. Moreover, a partnership is formed to act in the future and not in the past and when it is fully expected, intended and agreed that the incoming partner will render services to the partnership, the Government should not be heard to say: ‘I will not recognize you as a partner even though you in good faith entered into it. I took you into the Army to fight a war and you did not perform services for the partnership as you had agreed to do.’

“The inquiry as to a family partnership for income tax purposes must relate to evidence bearing on the reality, the actuality, and the bona fides of the transaction, or the absence thereof. Where the proof conclusively shows that a family partnership was entered into for the benefit of the business and not the purpose of evading, avoiding, or dividing, income taxes, it will be deemed a partnership for income tax purposes even as it is recognized in the law for all other purposes.

“Income generally should be taxed to him who owns it. The Culbertson boys owned one-half the cattle that produced the income here.

“Neither the Constitution, the statutes, nor public policy requires that partnerships between fathers and sons be outlawed or discouraged. The desire of a father in any age or clime, with a business that he cherishes and a son that he loves, to have such son with him in his business and to carry it on when he no longer can, was not rendered an anathema by the *Lusthaus* and *Tower* cases, and aberrations from the salutary rules announced in those cases should not now do so.” (*Italics supplied.*)

In *Kent v. Commissioner*, F. 2d (C. C. A. 6, September, 1948), the court commented on the Tax Court's attitude as follows:

"The Tax Court's construction of the *Tower* and *Lusthaus* cases, above mentioned, as well as the line of cases leading to the rule therein announced, is that lack of material income-producing services by the wife, or of capital originating with the wife, is sufficient to negative any partnership agreement between husband and wife, even in the absence of a finding of an underlying motive of tax reduction.

"However, in *Lawton et al. v. Commissioner*, 164 F. (2d) 380, this court held that these were only circumstances to be considered in determining whether family partnerships would be disregarded for tax purposes. . . ."

See also *Wilson v. Commissioner*, 161 F. 2d 661 (C. C. A. 7, April 30, 1947), where the following statement appears:

"The *Tower* and *Lusthaus* cases delineate the tests to be applied in determining whether the family partnership is a genuine partnership for Federal income tax purposes. *These tests are merely to aid in the ultimate determination of the existence of an actual, bona fide partnership.* . . ." (Italics supplied.)

Recently, even the Tax Court has apparently begun to recognize the error of its ways and to embrace the views expressed by the foregoing cases. Thus, in *Isaac Blumberg*, 11 T. C., No. 80 (October 25, 1948), that court approved the following as "a very good summary of the rationale of the Supreme Court's decision in the *Tower* and *Lusthaus* cases":

"The test in determining the bona fide character of a family partnership is to ascertain whether the

partners really and truly intended to join together for the purpose of carrying on a business and sharing in its profits, or whether the partnership was a mere sham utilized solely for the purpose of reducing a taxpayer's true tax liability by a pretended distribution of income."

Applying this test, the Tax Court recognized as a partner a son who contributed no capital of his own and who entered the armed services before the effective date of the partnership and rendered no substantial services during the taxable year.

In *William Collins, Sr.*, paragraph 48,241 P-H Memo T. C. (November 15, 1948), the court quoted with approval the foregoing statement from the *Blumberg* case and in *August J. Fischer*, paragraph 48,230 P-H Memo T. C. (October 25, 1948), the court referred to the "common sense proposition" that family partnerships are to be determined by the bona fides of the persons making up the partnership.

Accordingly, it seems crystal clear that the only question to be answered in this proceeding is: Did the petitioners and their children really and truly intend to join together for the purpose of carrying on a business and sharing its profits or losses, or was the arrangement merely a device for reducing income taxes?

The Tax Court in neither its Findings of Fact nor opinion made any specific finding as to the *intent* of the parties. Instead the court, in a confused opinion, appeared to question the validity of the initial gifts in one breath and to claim retention of control by petitioners in another.

The Tax Court dismissed the entire history of the parties, Albert's determination to enter the business, his special schooling to that end, his return to the business after discharge from the armed forces of the United States, all with the following statement:

"There is no evidence to clearly show that the usual terms of a partnership agreement were worked out so as to definitely establish the rights and duties of the son if he were to really carry on a business in partnership with his parents during the taxable years. The only inference which can be made from the record is that management of the business was to remain in Morris Harris, and that he was to continue to control the business and the earnings, as far as his children might be concerned. Partnership books were not closed. There were only bookkeeping entries which served to provide the basis for allocating earnings to the young son who was in school, at first, and later in the Army."

With respect to the daughter, Betty, the Tax Court says [Tr. 64]:

"There is no evidence that she desired to, or intended to, or did carry on the business enterprise in partnership with her parents in the taxable years. . . . There is no evidence of a completed transfer of an interest in the business to her such as would put her in complete dominion and control over an interest in the business and the earnings thereof. . . ."

With respect to Betty, the following should be noted:

(1) Petitioner Anna Harris testified at the hearing as follows [Tr. 88]:

"We also felt that as long as we were giving Albert a small share, just having the two children, we felt

it would be fair to give Betty the same share, and although she was very young, she always showed an interest. We felt that after her college, if she wasn't married, she would step in."

(2) Petitioners testified without equivocation that there were no restrictions as to the powers, rights of withdrawals, etc., of any of the partners. [Tr. 89.]

Against the Tax Court's meager and inadequate basis for striking down the partnership we may consider briefly the uncontroverted facts shown by the record. These facts show that the parties truly intended to enter into an honest, bona fide business relationship:

(1) We begin with an "integrated family enterprise" (*Lawton v. Commissioner, supra*). Petitioners, although husband and wife, had admittedly been real partners in the business in question for more than 20 years prior to 1943.

Under the circumstances what could be more natural and logical than that the children should likewise come into the business in order to carry it on after their parents' retirement.

(2) As early as 1937 Albert had indicated an active interest in the business and a desire to some day join his father and mother in its conduct. A possible sale of the business in 1937 was abandoned at Albert's request even though he was then very young.

(3) The testimony is unequivocal that after school hours and during vacations Albert always worked in the business. Thus, by the time the partnership was formed he had acquired a substantial familiarity with its operations.

(4) On at least two occasions prior to the formation of the partnership under attack Albert had asked petitioners for permission to quit school and devote all his energies to the business. On each occasion he was advised to continue his education with the assurance that he would thus become more valuable to the business.

Six months before the partnership was formed he had begun to take specialized courses looking especially to his entry into the business then being conducted by petitioners herein.

He returned to college in the fall and winter of 1942 as a result of the promise that he would become a partner on January 1, 1943. In attending a highly specialized textile school at the request of his partners, *Albert was performing a partnership service just as surely as if he had been present in person at the partnership's principal place of business.*

(5) Immediately upon his discharge from the armed forces, Albert returned to the business and has since devoted all his time thereto and performed substantial, vital, and important functions.

(6) With respect to Betty, a somewhat different situation exists. While it is true that at the time of the formation of the partnership it was unlikely that she would within the near future devote all her energies to the business, it was perfectly natural that having included the son, for perfectly valid business reasons, the parties would likewise include the daughter for a small interest.

(7) Finally, two extremely important factors, both of which were completely ignored by the Tax Court, should be carefully noted:

(a) The interests given by petitioners to their two children were extremely small—1/16th each. The parents thus recognized the inexperience of their young partners. What could be better evidence of the good faith of the petitioners herein than that they limited the participation of their children to these very small interests.

(b) As a part of (a) above it should be noted that the parties specifically testified that in connection with the formation of the partnership in question income taxes were neither considered nor even mentioned. It is obvious that had the parties been interested in minimizing taxes their children would have received far more substantial interests than were in fact given.

It is respectfully submitted that the authorities already cited indicate beyond doubt the true test applicable in determining the validity of a family partnership, namely, the intent of the parties.

By the same token, we believe that the record shows beyond question that there was here a bona fide intent to enter into an honest business relationship on the part of petitioners and their children.

It follows that the Tax Court's decision on the point in question was in error and should be reversed.

One further factor might be here briefly noted. The court is not bound to conclude that either both or none of the two children were bona fide partners. If the court should determine that a true intent to enter into a bona fide business relationship with Betty was lacking, it does not follow that the same decision should apply to Albert.

C. Income Taxes Paid to the State of California During the Year 1943 Are Deductible in Determining Petitioners' Respective Victory Tax Net Incomes for That Year.

Section 451(a)(3), *supra*, provides for the deduction of taxes in arriving at victory tax net income to the extent such taxes are paid or incurred in connection with the carrying on of a trade or business. It is respectfully submitted that state income taxes paid upon income derived from the operation of a trade or business are paid in connection therewith. If there is no income there is no tax. If there is income, there is a tax. The tax is the direct result of the income and if that income is derived from the operation of a business the tax thereon must necessarily be incurred in connection with the carrying on of that business.

Webster's New International Dictionary, Second Edition (Unabridged) defines the word "connection" as: "Relationship by causality, mutual dependence, logical sequence, or the like; relation of things when one of them is involved in another." The relationship between income from a business and the California income tax thereon is certainly one of cause and effect and the tax follows the income in a logical sequence. The tax here involved was, therefore, clearly paid in connection with the trade or business of the petitioners.

An analogous situation exists in connection with the determination of "adjusted gross income" for income tax

purposes as distinguished from "net income" for such purposes. In arriving at the former certain deductions attributable to a trade or business are allowable. In arriving at the latter, further purely personal expenses are allowed as deductions. Different ultimate tax consequences may result from the classification of deductions for said purposes.

In I. T. 3829, C. B. 46-2, p. 38, the respondent himself ruled that the Indiana gross income tax is deductible in arriving at adjusted gross income to the extent such tax is paid by an individual taxpayer on gross income derived from a trade or business. The only difference between the definition of deductions allowed in arriving at adjusted gross income and of those allowable in arriving at victory tax net income is that the former uses the words "attributable to" rather than "in connection with" a trade or business. There appears to be no reason for giving a different definition to the two phrases. If state income taxes can be said to be attributable to business income, then they can just as logically be said to be paid in connection with such trade or business.

This appears to be a case of first impression on the subject with the result that there are no case citations which are helpful. It is, therefore, submitted that the plain language of the statute indicates that in arriving at a victory tax net income a deduction should be allowed for state income taxes to the extent paid on income derived from a trade or business.

Conclusion.

Petitioners respectfully submit that the decision of the Tax Court should be reversed in its entirety for the reasons that the partnership was bona fide and not a tax avoidance scheme and that the California income taxes paid during 1943 were incurred in connection with the petitioners' trade or business.

Respectfully submitted,

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No. 12060

In the United States Court of Appeals
for the Ninth Circuit

ANNA HARRIS and MORRIS HARRIS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISIONS OF THE TAX
COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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**In the United States Court of Appeals
for the Ninth Circuit**

No. 12060

ANNA HARRIS and MORRIS HARRIS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

*ON PETITION FOR REVIEW OF THE DECISIONS OF THE TAX
COURT OF THE UNITED STATES*

BRIEF FOR THE RESPONDENT

OPINION BELOW

The findings of fact and opinion of the Tax Court (R. 51-71) are reported at 10 T. C. 818.

JURISDICTION

This petition for review involves income and victory taxes¹ for the years 1943 and 1944 in the respective amounts of \$5,662.73 and \$18,136.64 in the case of Anna Harris, and in the respective amounts of \$6,036.87 and \$18,693.10 in the case of Morris Harris. (R. 162-164.) On December 5, 1946, the Commissioner of Internal Revenue mailed notices of deficiencies to these taxpay-

¹ Although the Tax Court's decisions (R. 71-72) do not so indicate, the victory taxes are for only 1943 (R. 9, 33).

ers. (R. 8-9, 31-32.) Within ninety days thereafter, namely, on January 31, 1947 (R. 1, 17, 41), the taxpayers filed petitions with the Tax Court for the redetermination of such deficiencies pursuant to Section 272 of the Internal Revenue Code (R. 4-7, 27-30).

A motion to consolidate these cases was granted January 29, 1948. (R. 2.) Motion to file amended petitions was also granted February 11, 1948, and the amended petitions were filed on the same day. (R. 2, 19-24, 43-48.)

On May 12, 1948, the Tax Court entered its decisions sustaining the deficiencies as determined by the Commissioner. (R. 71-72.) Within three months thereafter, namely, on August 4, 1948, a petition for review by this Court was filed (R. 162-164) pursuant to the provisions of Section 1141 (a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948.

QUESTIONS PRESENTED

1. Whether the Tax Court correctly held that the taxpayers' son and daughter were not bona fide partners for income tax purposes in the partnership operating as Union Manufacturing Company, and that each of the taxpayers here, who are equal partners therein, is subject to tax, under Section 22 of the Internal Revenue Code, on one-half of the income of such partnership.

2. Whether, in computing their victory tax net income for 1943, as defined in Section 451 of the Internal Revenue Code, the taxpayers are entitled to deduct amounts paid as income taxes to the State of California.

STATUTE AND RULING INVOLVED

The pertinent provisions of the applicable statute and ruling are set out in the Appendix, *infra*.

STATEMENT

The pertinent facts as found by the Tax Court (R. 52-59) are as follows:

The taxpayers here are Morris Harris and Anna Harris. They are husband and wife, and residents of Los Angeles, California. Albert J. Harris and Betty Harris are their children and were nineteen and sixteen years old, respectively, in 1943, the first taxable year. (R. 52.)

The taxpayers had been associated together in the partnership known as the Union Manufacturing Company for many years prior to 1943, and each owned a one-half interest in such partnership under a written agreement which is dated April 1, 1937, and covers a term of ten years. (R. 52-53.)

Morris Harris began this enterprise in 1909, and has been the manager of the business, which is the manufacture and sale of work and sport clothes for men. The capital employed has been built up by retaining profits from year to year. In 1941 the volume of sales was around \$2,000,000. In 1942, about four hundred people were employed in the Los Angeles plant and in the El Paso, Texas, plant there were around one hundred people employed, but the employment in the latter plant increased later on to about three hundred. Morris Harris owns the land and building where the Los Angeles plant is located, and it does not appear as an asset in the balance sheet of the firm. In 1942 that plant and real estate had a value of around \$300,000, without equipment. The equipment which is used in the plant consists of all kinds of machinery and sewing machines. (R. 53.)

In the manufacturing departments there are several floor ladies under one superintendent. The goods manufactured are sold all over the United States. In

1942, the market was limited to the Rocky Mountain and Pacific Coast regions and ten or twelve salesmen were employed on a commission basis, but thereafter goods were sold in chain stores. Morris receives a salary of about \$200 a week which constitutes a drawing account against his share of the profits. (R. 53-54.)

As of December 31, 1942, the Union Manufacturing Company had assets of \$945,975.23, of which inventory amounted to \$538,992; and liabilities amounted to only \$9,065.40, leaving net assets of \$936,909.83. On that date, after the addition of one-half of 1942 profits, the balance of the capital account of Morris Harris was \$471,351.04; and the balance of the capital account of Anna Harris was \$465,558.79. (R. 54.)

The items on the balance sheet of the partnership as of December 31, 1942, are set forth in the record at pages 54-55.

The taxpayers' son Albert finished high school in June, 1941, and then attended the University of Virginia for one year. During the summer of 1942 he attended evening classes at the University of Southern California, where he took special courses in textiles. In September, 1942, he entered the textiles school of the University of North Carolina, and enlisted in the Army in December, 1942, but remained at the University until April, 1943, when he was called for active duty. (R. 55-56.)

The taxpayers' daughter Betty attended school during the years 1943 and 1944 either in high school or college. (R. 56.)

In 1942, in the summer months and at Christmas, taxpayers discussed the matter of making a gift of an interest in the partnership to their son, and considered it fair to do the same for their daughter. The arrangement discussed was not carried to any formal agreement. Thus there was no written agreement, and there

were no instruments of gifts or assignments or transfers drawn up or executed. In the discussions, Anna Harris was to make a gift of a part of her partnership interest to her son and Morris Harris was to make a gift of part of his interest to his daughter. The gifts were to be made on or about January 2, 1943. (R. 56.)

On September 16, 1943, book entries were made in the capital accounts of Anna and Morris Harris, and ledger sheets were made opening capital accounts in the names of Albert and Betty. However, the book entries did not show that the transfers were made as the parties had intended, nor did the entries correspond with the two gift tax returns of the taxpayers which were dated September 27, 1943. Instead, the capital account of Morris Harris was debited on September 16, 1943, with the amount \$34,083.70, and a capital account in the name of Albert Harris was credited with the same amount as of January 1, 1943, by a transfer from the capital account of Morris Harris. Also, the capital account of Anna Harris was debited on September 16, 1943, in the amount of \$34,083.70; and a capital account in the name of Betty Harris was credited with the same amount as of January 1, 1943, by transfer from the capital account of Anna Harris. (R. 56-57.)

The business of Union Manufacturing Company was conducted during 1943 and 1944 in the same way as it had been conducted in 1942 and prior years. No services were rendered to or in the business by the children, Albert and Betty, during 1943 and 1944, and neither contributed any capital of his own to the existing partnership business in those years or earlier years. (R. 58.)

When, prior to 1943, Albert went to the place of business to do work of some general type which a school boy could do, after school hours and during school vacations, he was not paid any amount. (R. 58.)

Neither Albert nor Betty withdrew any sum from the Union Manufacturing Company during 1943 and 1944. However, debits to each of their capital accounts were made at the end of 1942 and 1943 for taxes on income which was attributed to each one under bookkeeping entries made in their capital accounts. At the end of 1943 and 1944, each of these capital accounts was credited with one-sixteenth of the earnings for each year. At the end of 1943, the balance in each of their capital accounts was \$46,074.86. (R. 58.)

The Tax Court found that Albert and Betty Harris were not bona fide members of the partnership here in 1943 and 1944 and that there continued to be only two partners in those years. (R. 59.)

Personal income taxes for the year 1942 were paid to the State of California by Morris Harris in the amount of \$26,746.65, and by Anna Harris in the amount of \$25,256.18. In computing their victory tax liability for the year 1943, taxpayers deducted the above amounts of California tax in their respective returns. The Commissioner disallowed each deduction in determining each taxpayer's net income subject to 1943 victory tax. (R. 59.) The Tax Court approved the Commissioner's determination on this issue. (R. 66-71.)

SUMMARY OF ARGUMENT

1. The question of whether the taxpayers' son and daughter can be treated as partners for income tax purposes during 1943 and 1944 depends on whether the taxpayers (who were already equal partners in an established business) and their two minor children intended to carry on a partnership business. The legal principles applicable here have been announced in many decisions holding that the so-called family partnership, although it may be valid under state laws, will not be recognized for income tax purposes if the arrange-

ment produces no real change in the conduct of the business and in the creation of the income therefrom but results merely in a reallocation of the income within the family unit. These cases point out further that in determining the question here, the Tax Court should consider the agreement of the parties and their conduct thereunder, giving particular attention to whether the alleged partners (i.e., the son and daughter here) have contributed any capital originating with them, whether they have contributed substantially to the management and control of the business and whether they have performed any vital additional services.

In applying these established principles, the Tax Court found that the children here had made none of the required contributions, that after an interest in the partnership was allegedly given to the children by their parents, the business of the partnership was carried on exactly as before, and that the parents continued to be the owners of the partnership. Consequently, the Tax Court properly held that the children should not be recognized as partners for income tax purposes during the taxable years.

2. The taxpayers also claim that in computing their victory tax net income for 1943, they are entitled to deduct the California income tax which they paid. The statute allows a taxpayer, in making such computation, to deduct taxes only to the extent that they are paid or incurred in carrying on a trade or business, or in connection with property used in business or in the production of income. The California income tax does not come in any of these categories. Thus the Tax Court correctly denied the deductions claimed by the taxpayers.

ARGUMENT

I

The Taxpayers' Children Were Not Bona Fide Partners for Income Tax Purposes in the Union Manufacturing Company During the Taxable Years, and the Income Therefrom Which Is Claimed by Them Should Be Treated for Income Tax Purposes as Belonging to Their Parents

The first issue in this case is whether the portion of the income of the Union Manufacturing Company attributed to Albert and Betty Harris, son and daughter of the taxpayers here, was includible in the gross income of the latter for the taxable years 1943 and 1944 under the provisions of Section 22 (a) of the Internal Revenue Code (Appendix, *infra*). The Tax Court held that Albert and Betty Harris were not bona fide partners for tax purposes during those years, and that their parents were taxable on all the income from the above company.

This case follows the usual pattern of the "family partnership" cases and actually differs in no material respect from many other cases which have been decided by the Supreme Court,² by this Court,³ and other Courts of Appeals⁴ against the claims of taxpayers who have

² *Commissioner v. Tower*, 327 U.S. 280, and *Lusthaus v. Commissioner*, 327 U.S. 293, are considered the controlling cases on this issue.

³ *Nordling v. Commissioner*, 166 F. 2d 703, certiorari denied, 335 U.S. 817; *Quon v. Commissioner*, 165 F. 2d 215, certiorari denied, 334 U.S. 845.

⁴ See e.g., Second Circuit: *Seifert v. Commissioner*, 157 F. 2d 719; *Seibert v. Commissioner*, 156 F. 2d 227; *Miller v. Commissioner*, 150 F. 2d 823; *Waldburger v. Helvering*, 131 F. 2d 598. Third Circuit: *Eisenberg v. Commissioner*, 161 F. 2d 506, certiorari denied, 332 U.S. 767; *Davis v. Commissioner*, 161 F. 2d 361; *Walker v. Commissioner*, 160 F. 2d 313. Fourth Circuit: *Wilson v. Commissioner*, 161 F. 2d 556, certiorari denied, 332 U.S. 769; *Mauldin v. Commissioner*, 155 F. 2d 666; *Hash v. Commissioner*, 152 F. 2d 722, certiorari denied, 328 U.S. 838, rehearing denied, 328 U.S. 879; *Economos v. Commissioner*, 167 F. 2d 165, certiorari denied, 335 U.S. 826. Fifth Circuit: *Scherf v. Commissioner*, 161 F. 2d 495,

unsuccessfully advanced many ingenious arguments why their wives, children, or other members of their families should be recognized as their partners for tax purposes under Sections 22, 181, 182, and 183 of the Internal Revenue Code (Appendix, *infra*).

These cases hold that a family partnership based upon the transfer of so-called partnership interests from a taxpayer to his wife or other members of his family is not entitled to recognition, for income tax purposes, even though valid under state law and as to third parties, if the arrangement produces no change in the conduct of the business and in the creation of the income therefrom, but amounts merely to a reallocation of income among members of the family involved. In discussing the principles to be applied in such cases, the Supreme Court stated in *Commissioner v. Tower*, 327 U. S. 280, 286-287, 289:

A partnership is generally said to be created when persons join together their money, goods, labor, or skill for the purpose of carrying on a trade, profession, or business and when there is community of interest in the profits and losses. When the existence of an alleged partnership arrangement is challenged by outsiders, the question

certiorari denied, 332 U.S. 810; *Benson v. Commissioner*, 161 F. 2d 821; *Belcher v. Commissioner*, 162 F. 2d 974, certiorari denied, 332 U.S. 824; *Mead v. Commissioner*, 131 F. 2d 323, certiorari denied, 326 U.S. 762; *Blalock v. Allen*, 151 F. 2d 927. Sixth Circuit: *Hougland v. Commissioner*, 166 F. 2d 815, certiorari denied, 334 U.S. 846; *Weinstein v. Commissioner*, 166 F. 2d 81; *Dawson v. Commissioner*, 163 F. 2d 664; *Lowry v. Commissioner*, 154 F. 2d 448, certiorari denied, 329 U.S. 725; *Lorenz v. Commissioner*, 148 F. 2d 527, certiorari denied, 327 U.S. 786; *Thorrez v. Commissioner*, 155 F. 2d 791; *Epps v. Commissioner*, 164 F. 2d 482. Seventh Circuit: *Appel v. Smith*, 161 F. 2d 121; *Tinkoff v. Commissioner*, 120 F. 2d 564. Eighth Circuit: *Doll v. Commissioner*, 149 F. 2d 239, certiorari denied, 326 U.S. 725; *Supornick v. Commissioner*, 150 F. 2d 110. Tenth Circuit: *Earp v. Jones*, 131 F. 2d 292, certiorari denied, 318 U.S. 764; *Grant v. Commissioner*, 150 F. 2d 915; *Bradshaw v. Commissioner*, 150 F. 2d 918; *Losh v. Commissioner*, 145 F. 2d 456.

arises whether the partners really and truly intended to join together for the purpose of carrying on business and sharing in the profits or losses or both. *And their intention in this respect is a question of fact, to be determined from testimony disclosed by their "agreement, considered as a whole, and by their conduct in execution of its provisions."* * * * We see no reason why this general rule should not apply in tax cases where the Government challenges the existence of a partnership for tax purposes.

* * * * *

The issue is who earned the income and that issue depends on whether this husband and wife really intended to carry on business as a partnership. (Italics supplied.)

Thus the primary issue in family partnership cases, as in all tax cases, is who earned the income, and in order to treat members of a family as partners for tax purposes it must be found that they actually intend to carry on the business as partners. To determine such intent the Tax Court should examine not only the agreement of the parties but also their conduct in carrying it out. In this connection, the Supreme Court called attention in the *Tower* case (p. 290) to three tests which the Tax Court should consider and apply in the course of its examination of the facts, namely, (1) whether the wife (the alleged partner in that case) contributed any capital originating with her, (2) whether she contributed substantially to the management and control of the business in the taxable years, and (3) whether she performed any vital additional services in those years. Under the ruling in the *Tower* case, it is clear that if the Tax Court finds, as it found here, that the alleged partners have not made any of these contributions, then it may properly decide that such persons should not be treated as partners for income tax purposes.

As counsel appear to object to the application of the above tests to the facts here, we take the liberty of referring in some detail to other statements in the *Tower* case which indicate that counsel do not correctly interpret that case, as well as other cases cited herein. It will be seen that counsel not only state (Br. 20) that the three tests listed in the *Tower* case are “merely *some* of the facts to be considered in arriving at an ultimate decision,” but also seem to take the position that even when no contributions of capital or services are made by the alleged partners, the Tax Court may still find that the parties intend to carry on a business as a partnership if there has been a valid gift of an interest in the business to the alleged partners. But, in taking such a position, we submit that counsel have failed to give due significance not only to the general principles governing partnerships but also to what matters the Tax Court may properly consider in determining the question as to the intent of the alleged partners. That the contributions of the alleged partners may be determinative of such question was clearly indicated by the Supreme Court in the *Tower* case when it said (p. 290) :

There can be no question that a wife and a husband may, under certain circumstances, become partners for tax, as for other, purposes. If she either invests capital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, or does all of these things she may be a partner as contemplated by 26 U. S. C. §§ 181, 182. * * * *But when she does not share in the management and control of the business, contributes no vital additional service, and where the husband purports in some way to have given her a partnership interest, the Tax Court may properly take these circumstances into consideration in determining whether the partnership is real within*

the meaning of the federal revenue laws. (Italics supplied.)

Thus the Supreme Court held that in deciding the issue here the Tax Court *may properly* take into consideration whether the alleged partner has rendered services and contributed capital; and it follows from what was said in the *Tower* case, and the other cases cited herein, that when no vital services have been rendered and no capital contributed, the Tax Court may properly find that the parties did not intend to carry on the business as a partnership and are not partners for tax purposes. Consequently, the Tax Court was fully within its authority when it applied the three tests listed above to the facts of this case; and it did not have to consider other facts since all three of the tests referred to are absent here. But, as we shall point out below, the Tax Court did consider other facts and, on the basis of all the facts, reached the conclusion that the children could not be treated as partners for tax purposes.

It appears that the primary reason for the different view adopted by the taxpayers is that they have failed to recognize the basic issue in such cases as this although such issue was emphasized throughout the opinion in the *Tower* case. As to this, the Supreme Court said (pp. 283, 290-292):

And we have held *that the dominant purpose of all sections of the revenue laws, including these, is "the taxation of income to those who earn or otherwise create the right to receive it and enjoy the benefit of it when paid."* * * * *The basic question in deciding whether the Commissioner's deficiency assessment was proper, is: Was the income attributed to the wife as a partner income from a partnership for which she alone was liable in her "individual capacity," * * * or did the husband, despite the claimed partnership, actually*

create the right to receive and enjoy the benefit of the income, so as to make it taxable to him under §§ 11 and 22 (a) ?

* * * * *

*It is the command of the taxpayer over the income which is the concern of the tax laws. * * **
 And income earned by one person is taxable as his, if given to another for the donor's satisfaction.
 * * *

Judged by the actual result achieved, the Tax Court was justified in finding that the partnership here brought about no real change in the economic relation of the husband and his wife to the income in question. * * * After the partnership was formed the husband continued to control and manage the business exactly as he had before. * * * *No capital not available for use in the business before was brought into the business as a result of the formation of the partnership. * * * Consequently the result of the partnership was a mere paper reallocation of income among the family members. The actualities of their relation to the income did not change. (Italics supplied.)*

It is clear from the above statement that in determining the question here, the Tax Court was required to decide who had actually earned the income either by contributing property or by rendering services. Moreover, when the capital used in the business after the formation of the alleged partnership is exactly the same as that available previously, alleged partners, who may have title to a share of such capital by reason of a gift, will not be treated for tax purposes as having made a contribution to capital.

The facts here show that the taxpayers' children did not contribute any capital originating with themselves; they did not help in the management or control of the business and neither rendered any services. (R. 58, 112.) The daughter was 16 years old in 1943; she at-

tended school during both taxable years and rendered no services of any kind to the Union Manufacturing Company. (R. 52, 56, 64, 106.) It is also not disputed that the son rendered no services to the business during the years here involved. He was only 19 in 1943, and was in college until April of that year when he was called for active duty in the armed forces and remained in the Army throughout the remainder of the taxable period here. (R. 52, 55-56, 91-92, 115-117.) It is true that the son was interested in textiles and had done some work around the plant and office of the Union Manufacturing Company, but these jobs were done without pay and always during vacations. Moreover, such services were entirely before the taxable years and were not substantial or important. (R. 55, 65.)

In view of these undisputed facts, the Tax Court properly found that neither of the children had made any of the contributions referred to in the *Tower* case, *supra*. But, in reaching its conclusion that the parties did not actually intend for the children to join in the business as partners, the Tax Court also considered other facts. These include the youthfulness and inexperience of the children, which we have just referred to, also the fact that when partnership interests were allegedly given to the children no new capital was added to that which the parents had previously supplied, and the fact that the father, as manager, continued to carry on the business exactly as before the alleged gifts were made.

In this connection, the Tax Court also noted that there was no written partnership agreement (R. 88-89), nor was there any formal transfer of any interest in the business to the children. There were entries in the books of the partnership between Mr. and Mrs. Harris indicating that a capital account was set up for each of the children on September 16, 1943. But, as the Tax

Court pointed out (R. 66), there is no evidence to show just what were the terms of the alleged oral agreement with the children, but it can be inferred from the conduct of the business thereafter that it was to be run as before with Mr. Harris acting as manager and in control. This conclusion of the Tax Court is substantiated by the testimony of Mrs. Harris who stated that she was familiar with the business, that it was operated in the same manner in the taxable years as it always had been, and that her son performed no services in 1943 and 1944. (R. 103-105.)

In view of what has already been said herein, we do not consider it necessary to reply to the taxpayers' assertion (Br. 16) that the Tax Court made no specific finding as to the validity of the gifts, and erred in not doing so. Actually, the Tax Court did consider "whether bona fide gifts in praesenti were made" (R. 60) and, after a discussion of the facts, both as to Betty and Albert, the Tax Court held specifically that the evidence was not sufficient to show that a bona fide gift of a present interest in the business had been made to either one (R. 64-66). However, we repeat that the important factor here is not whether valid gifts were made but whether the parties actually intended for the children to join in the partnership business.

It may be, now that Albert is actually participating in the business, after a three-year absence in the Army (R. 118), that he could be considered as a partner today but that is not the question before us here. Our question is whether Albert and his sister Betty were partners in 1943 and 1944. It seems to be conceded by counsel that the situation is different as to Betty and that the facts are weaker as to her. (Br. 29.) But we submit that the facts do not show that either one was a partner in our taxable years or that they intended to be.

The taxpayers rely on the fact that Albert was interested in textiles and had expressed the wish to help his father carry on the business. Yet it was at their earnest solicitation that he decided to continue his college studies rather than go into the business. Because he made that decision Mrs. Harris said that they gave him an interest in the business but only as an inducement for him to go on to school. (R. 87.) This is also brought out in Albert's testimony when he explained that he had talked with his father about going into the business and in December, 1942 "was anxious to go in then", but that his parents wanted him to go back to school. As to this he said, "they said they would give me this, but I had to go back though for at least another year. * * * it was understood I would go back until at least, I had a knowledge so I could go about the business". (R. 120-121.) Clearly, this testimony, even when given the most favorable interpretation for the taxpayers, shows that they did not intend for Albert to come into the business immediately. Moreover, Albert joined the Army in December, 1942 (R. 55), so it was known long before the book entries were made in September, 1943, or anything else was done about the alleged partnership with the children that Albert would be prevented by his Army service from actually participating in the business then. Cf. *Davis v. Commissioner*, 161 F. 2d 361 (C. A. 3d).

The taxpayers have cited a number of cases which they assert support their position here. However, these are distinguishable on their facts with the possible exception of *Culbertson v. Commissioner*, 168 F. 2d 979 (C. A. 5th), but this case is now pending in the Supreme Court on a writ of certiorari granted December 6, 1948. It should also be noted that even though it was held that the father there was in partnership with his sons who intended to participate in the busi-

ness at some future time, it was recognized that the daughter, who also received a share of the business, was not a partner as it was not intended that she would ever contribute any services or capital thereto. As to the situation of minor children, also see *Wilson v. Commissioner*, 161 F. 2d 556 (C. C. A. 4th), certiorari denied, 332 U. S. 769.

It should also be noted that in *Lawton v. Commissioner*, 164 F. 2d 380 (C. C. A. 6th), the children had rendered valuable services to the business involved there, and in *Wilson v. Commissioner*, 161 F. 2d 661 (C. C. A. 7th), it was decided that the taxpayer's wife was a partner because she had contributed important services and money of her own. Thus, in both of these cases, on which the taxpayers rely, the courts were careful to apply the tests laid down in the *Tower* case, and to point out that the parties met such tests and did intend to carry on the business as a partnership. Such tests were also applied by this Court in *Nordling v. Commissioner*, 166 F. 2d 703, certiorari denied, 335 U. S. 817, in which it was found that the wife was not a partner for income tax purposes since she had contributed no capital of her own and had rendered only negligible services to the business.

II

State Income Taxes Are Not Deductible in Computing Victory Tax Net Income

The Commissioner determined that the taxpayers are not entitled to deduct the amount of California income tax which they paid in computing the amount of their victory tax net income in 1943. The Tax Court upheld the Commissioner's determination on this issue also.

Victory tax net income is defined in Section 451 (a) of the Internal Revenue Code (Appendix, *infra*) as gross income (with certain exceptions not material

here) minus the sum of the deductions listed therein and including taxes as follows:

Amounts allowable as a deduction by section 23 (c), to the extent such amounts are paid or incurred in connection with the carrying on of a trade or business, or in connection with property used in the trade or business, or in connection with property held for the production of income.

Taxes which may be deducted under Section 23 (c) (Appendix, *infra*), referred to above, include all taxes except certain ones listed therein. Thus, since state income taxes are not listed as one of the exceptions, they can be deducted under Section 23 (c) in computing ordinary net income. But, obviously, to compute victory tax net income under Section 451(a), it is necessary to consider something in addition, namely, it must also be shown that the state income taxes involved were paid or incurred (1) in connection with the carrying on of a trade or business, or (2) in connection with property used in the trade or business, or (3) in connection with property held for the production of income. In holding that the California income taxes could not be deducted here, the Tax Court stated (R. 68-69) :

It is our understanding that the California income tax is a personal income tax which, like the Federal income tax, is imposed upon income derived from all sources. * * * Petitioners argue that the state income tax was a tax which was paid or incurred in connection with the carrying on of a business within the meaning of section 451 (a)(3) because the income which was taxed by the state was derived from a business.

The construction which the petitioners would have placed upon section 451 (a)(3) does not, in our opinion, give proper consideration to the wording of the pertinent section. The state income tax was not incurred "in connection with the carry-

ing on of the business.” Those words have a clear meaning, but, if it is necessary to undertake to clarify them, we think that the words mean a tax which is incurred as an incident to the carrying on of business in the sense that a business expense is incurred in carrying on a business; that is to say, something which must be paid in order to do business.

We submit that the Tax Court correctly interpreted the statute. As this Court undoubtedly knows, the California statute, under which the taxpayers paid income tax to that state in 1943, was entitled “The Personal Income Tax” (3 Deering’s California General Laws, Act 8494) and contained many provisions very similar to those found in the federal income tax law. This is particularly true as to the definitions of net and gross income, and as to its treatment of partnerships (see Sections 6.7 and 22 of Act 8494 of Deering’s California General Laws, *supra*). Thus it seems evident, as the Tax Court held, that the California income tax is a personal income tax like the federal income tax and is imposed on income from all sources. Accordingly, we submit it is not a tax which is paid as an incident to carrying on a business and does not come within any of the provisions of Section 451 (a), referred to above.

It does not appear that the specific question here has been involved in any other case. However, in enacting the provisions of Section 451 (a), the Committee on Finance (S. Rep. No. 1631, 77th Cong., 2d Sess., p. 8 (1942-2 Cum. Bull. 504, 509)) made the following significant comment in regard to it:

Since the Victory tax does not allow any deduction for State income taxes, your committee deemed it advisable to provide that the total income tax and Victory tax should not exceed 90 per cent of the taxpayer’s net income.

Also see I. T. 3644, 1944 Cum. Bull. 372-373 (Appendix, *infra*), in which it was held that personal income taxes are not deductible in computing victory tax net income under Section 451 (a).

The taxpayers rely on another ruling of the Commissioner (I. T. 3829, 1946-2 Cum. Bull. 38) in which it was held that a taxpayer might deduct such portion of the Indiana gross income tax as was attributable to a trade or business. But it should be noted that I. T. 3829 referred to the computation of "adjusted gross income"⁵ and here we are concerned with a different computation, namely, the computation of "victory tax net income". These are technical terms referring to sums which must be computed exactly as the statute indicates. Thus it does not follow that what may be done in making one computation may be done in the other. Moreover, as we have already pointed out, it was not the intention of Congress to allow state income taxes to be deducted in computing victory tax net income. However, even if we are wrong in our interpretation of Section 451 (a) and a state income tax can be properly deducted, it still must be shown that such tax is paid or incurred as an incident to the carrying on of a trade or business, and the taxpayers have not done so. Counsel merely assert (Br. 31) that state income taxes paid upon income derived from the operation of a business are paid in connection with the carrying on of such business but they point to no evidence here showing the source of the income on which the state taxes here

⁵ That term is defined in Section 22 (n) of the Internal Revenue Code, as added by Section 8 (a) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231, as gross income minus certain deductions including—

(1) *Trade and business deductions*.—The deductions allowed by section 23 which are attributable to a trade or business carried on by the taxpayer, if such trade or business does not consist of the performance of services by the taxpayer as an employee; * * *.

were paid. While it may be true that most of the income here was derived from the partnership business, neither the federal nor state personal income tax return was produced and there is no evidence to support the taxpayers' claim that the tax was paid in connection with any business.

Accordingly, the deduction was properly denied.

CONCLUSION

The decisions of the Tax Court are correct on both issues and should be affirmed.

Respectfully submitted,

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FEBRUARY, 1949.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition*.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 22.)

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(c) [as amended by Sec. 202 of the Revenue Act of 1941, c. 412, 55 Stat. 687; Secs. 105, 122 and 158 of the Revenue Act of 1942, c. 619, 56 Stat. 798; and Sec. 111 of the Revenue Act of 1943, c. 63, 58 Stat. 21] *Taxes Generally*.—

(1) *Allowance in general*.—Taxes paid or accrued within the taxable year, except—

(A) Federal incomes taxes;

(B) war-profits and excess-profits taxes imposed by Title II of the Revenue Act of 1917, Title III of the Revenue Act of 1918, Title III of the Revenue Act of 1921, section 216 of the National Industrial Recovery Act,

or section 702 of the Revenue Act of 1934, or Subchapter E of Chapter 2, or by any such provisions as amended or supplemented;

(C) income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States, if the taxpayer chooses to take to any extent the benefits of section 131;

(D) estate, inheritance, legacy, succession, and gift taxes;

(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; and

(F) Federal import duties, and Federal excise and stamp taxes (not described in subparagraph (A), (B), (D), or (E)), but this subsection shall not prevent such duties and taxes from being deducted under subsection (a).

(3) *Retail sales tax*.—In the case of a tax imposed by any State, Territory, District, or possession of the United States, or any political subdivision thereof, upon persons engaged in selling tangible personal property at retail, which is measured by the gross sales price or the gross receipts from the sale or which is a stated sum per unit of such property sold, or upon persons engaged in furnishing services at retail, which is measured by the gross receipts for furnishing such services, if the amount of such tax is separately stated, then to the extent that the amount so stated is paid by the purchaser (otherwise than in connection with the purchaser's trade or business) to such person such amount shall be allowed as a deduction in computing the net income of such purchaser as if such amount consti-

tuted a tax imposed upon and paid by such purchaser.

* * * *

(26 U. S. C. 1946 ed., Sec. 23.)

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

(26 U. S. C. 1946 ed., Sec. 181.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * *

(26 U. S. C. 1946 ed., Sec. 182.)

SEC. 183. [as amended by Sec. 9 of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231].

COMPUTATION OF PARTNERSHIP INCOME.

(a) *General Rule.*—The net income of the partnership shall be computed in the same manner and on the same basis as in the case of an individual, except as provided in subsections (b), (c), and (d).

* * * *

(26 U. S. C. 1946 ed., Sec. 183.)

SEC. 451 [as added by Sec. 172 of the Revenue Act of 1942, *supra*]. VICTORY TAX NET INCOME.

(a) *Definition.*—The term “victory tax net income” in the case of any taxable year means (except as provided in subsection (c)) the gross income for such year (not including gain from the sale or exchange of capital assets as defined in section 117, or interest allowed as a credit against net income under section 25 (a)(1) and (2), or

amounts received as compensation for injury or sickness which are included in gross income by reason of the exception contained in section 22 (b) (5)) minus the sum of the following deductions:

* * * * *

(3) *Taxes*.—Amounts allowable as a deduction by section 23 (c), to the extent such amounts are paid or incurred in connection with the carrying on of a trade or business, or in connection with property used in the trade or business, or in connection with property held for the production of income.

* * * * *

I. T. 3644, 1944 Cum. Bull. 372-373:

Advice is requested as to the deductibility, in computing victory tax net income, of the personal income taxes imposed by the various States.

In computing victory tax net income, amounts of taxes allowable as a deduction by section 23 (c) of the Internal Revenue Code may be deducted under section 451 (a) (3) of the Code, as added by section 172 (a) of the Revenue Act of 1942, "to the extent such amounts are paid or incurred in connection with the carrying on of a trade or business, or in connection with property used in the trade or business, or in connection with property held for the production of income."

That Congress intended to restrict, for victory tax purposes, the deductions ordinarily allowed by section 23 (c) of the Code is evident from the language of section 451 (a) (3) of the Code, *supra*, and the report submitted by the Committee on Finance of the Senate (Senate Report No. 1631, Seventy-seventh Congress, second session, C. B. 1942-2, 504, at page 509), on the revenue bill of 1942, in which it is stated, in part, as follows:

Since the victory tax does not allow any deduction for State income taxes, your committee deemed it advisable to provide that the total in-

come tax and victory tax should not exceed 90 per cent of the taxpayer's net income. * * *
[Italics supplied.]

It is held, therefore, that the personal income taxes imposed by the various States are not deductible in whole or in part in computing victory tax net income under section 451 (a) (3) of the Internal Revenue Code, *supra*.

No. 12060

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ANNA HARRIS and MORRIS HARRIS,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF FOR PETITIONERS.

FILED

FEB 24 1949

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Respondent Confuses the Partnership Issue.

The Respondent, at pages 8 and 9 of his brief, has cited a long list of cases which he claims support his statement that "this case follows the usual pattern" of family partnership cases. There are several points in this connection which merit further discussion by the Petitioners.

It has been said many times by the Courts that these partnership cases are each to be decided on its own facts and that the citation of cases is not particularly helpful. We have already cited those cases which we believe estab-

lish the correct rules to be followed in arriving at a decision here and it would be a waste of the Court's time to analyze the Respondent's cases individually.

All of the cited cases arose under the old Dobson rule (*Dobson v. Commissioner*, 320 U. S. 489) which limited the right of the appellate court in its review of the facts. This rule has now been changed by Congressional action (Public Law No. 773, section 36) so that decisions of the Tax Court are now reviewable to the same extent as those of the District Court in non-jury civil actions.

The foregoing comments are particularly applicable to the two cases cited from this Circuit. In *Nordling v. Commissioner*, 166 F. 2d 703, this Court, referring to the findings of the Tax Court, said, "These findings are supported by evidence and we are without authority to overturn them." *Quon v. Commissioner*, 165 F. 2d 215, was affirmed without opinion. Furthermore, these cases are clearly distinguishable from ours on the facts.

Nordling, in exercising an option to buy his partner's interest in the business, instructed his attorney to insert his wife's name in the contract as a co-purchaser and followed by making her a partner. It appears this was done on the advice of a tax consultant purely for the purpose of reducing income taxes. In our case, the partnership was formed following discussions extending over a period of several months, and the record is clear that its effect on income taxes was given no consideration whatsoever.

An examination of the memorandum decision of the Tax Court in the *Quon* case, found at paragraph 47,077 of the 1947 Prentice-Hall Tax Court Memorandum Decisions service, reveals that the purpose and intent of the parties was, through the creation of trusts as partners, to provide security for children aged 11, 9, 5, and 4 years, respectively, to transfer title to a substantial part of the business to citizens in order to forestall freezing of the assets belonging to an alien, and to reduce income taxes.

Thus, in neither cases did there appear a bona fide intention to carry on business as partners, whereas the undisputed evidence in our case is that such was the intention.

The Respondent has thoroughly confused the principles to be gleaned from the Supreme Court decisions in *Commissioner v. Tower*, 327 U. S. 280, and *Lusthaus v. Commissioner*, 327 U. S. 293. After referring to the statement that the absence of capital or services contributed by the questioned partner are circumstances which may properly be considered by the Tax Court, he draws the unwarranted conclusion that they are the only circumstances which need be considered. As already pointed out in Petitioners' opening brief, supported by several cases, the issue is not so limited.

The Respondent, in attempting to distinguish, on the facts, the cases cited by Petitioners in their opening brief, not only misses the point, but ignores completely the recent Tax Court decisions in *Isaac Blumberg*, 11 T. C., No. 80, *William Collins, Sr.*, para. 48,241 P-H Memo T. C.,

and *August J. Fischer*, para. 48,230 P-H Memo T. C. cited at pages 25 and 26 of Petitioners' opening brief.

The purpose of citing authorities in a case such as this, which is to be decided on its own peculiar facts, is to establish a rule to be applied to those facts. The cases cited by Petitioners do just that. They show beyond question that the decision is to be controlled by the bona fide intention of the parties as revealed by the entire record and not by three elements alone.

The Victory Tax Issue.

No further comment is required on this issue, on which there is no case authority and which is controlled by the clear language of the statute.

Conclusion.

The decisions of the Tax Court on both issues are incorrect and should be reversed.

Respectfully submitted,

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